DOCKET

SUPREME COURT
OF THE UNITED STATES

No. 10-179
Title: Howard K. Stern, Executor of the Estate of Vickie Lynn Marshall, Petitioner
v.
Elaine T. Marshall, Executrix of the Estate of E. Pierce Marshall
Docketed: August 5, 2010
Lower Ct: United States Court of Appeals for the Ninth Circuit
Case Nos.: (02-56002, 02-56067)
Decision Date: March 19, 2010
Rehearing Denied: May 5, 2010
Questions Presented

---Date---	--------Proceedings and Orders----------
Aug 3 2010	Petition for a writ of certiorari filed. (Response due September 7, 2010)
Aug 20 2010	Brief of respondent Elaine T. Marshall, Executrix of the Estate of E. Pierce Marshall in opposition filed.
Aug 31 2010	Reply of petitioner Howard K. Stern, Executor of the Estate of Vickie Lynn Marshall filed. (Distributed)
Sep 1 2010	DISTRIBUTED for Conference of September 27, 2010
Sep 28 2010	Petition GRANTED limited to Questions 1, 2, and 3 presented by the petition.
Nov 2 2010	Consent to the filing of amicus briefs, in support of either party or of neither party, received from counsel for the petitioner.
Nov 2 2010	Consent to the filing of amicus briefs, in support of either party or of neither party, received from counsel for the respondent.
Nov 8 2010	SET FOR ARGUMENT ON Tuesday, January 18, 2011
Nov 12 2010	Joint appendix filed. (Statement of costs filed)
Nov 12 2010	Brief of petitioner Howard K. Stern, Executor of the Estate of Vickie Lynn Marshall filed.
Nov 15 2010	Brief amici curiae of Professors Richard Aaron, et al. filed.
Nov 19 2010	Brief amicus curiae of National Association of Bankruptcy Trustees filed.
Nov 19 2010	Brief amicus curiae of the United States filed.
Nov 24 2010	Motion of the Acting Solicitor General for leave to participate in oral argument as amicus curiae and for divided argument filed.
Nov 26 2010	CIRCULATED.
Dec 2 2010	Record received from U.S.C.A. for 9th Circuit. (1 box)
Dec 13 2010	Brief of respondent Elaine T. Marshall, Executrix of the Estate of E. Pierce Marshall filed. (Distributed)
Dec 16 2010	Record received from U.S.D.C. for Central District of California. (36 boxes)
Dec 20 2010	Brief amicus curiae of Washington Legal Foundation filed. (Distributed)
Dec 20 2010	Brief amici curiae of Law Professors S. Todd Brown, et al. filed. (Distributed)
Dec 20 2010	Brief amici curiae of National Black Chamber of Commerce, et al. filed. (Distributed)
Dec 20 2010	Brief amicus curiae of Center for the Rule of Law filed. (Distributed)
Jan 7 2011	Motion of the Acting Solicitor General for leave to participate in oral argument as amicus curiae and for divided argument GRANTED.
Jan 11 2011	Reply of petitioner Howard K. Stern, Executor of the Estate of Vickie Lynn Marshall filed. (Distributed)
Jan 18 2011	Argued. For petitioner: Kent L. Richland, Los Angeles, Cal.; and Malcolm L. Stewart, Deputy Solicitor General, Department of Justice, Washington, D. C. (for United States, as amicus curiae.) For repondent: Roy T. Englert, Jr., Washington, D. C.

PETITION FOR WRIT OF CERTIORARI

Supreme Court, U.S.
FILED

No.

10-179 AUG 3 - 2010

In the

Supreme Court of the United States

OFFICE OF THE CLERK

HOWARD K. STERN, EXECUTOR OF
THE ESTATE OF VICKIE LYNN MARSHALL,

Petitioner,

v.

ELAINE T. MARSHALL, EXECUTRIX OF
THE ESTATE OF E. PIERCE MARSHALL,

Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

In the 1984 Bankruptcy Act, Congress divided bankruptcy court jurisdiction into "core" proceedings, in which bankruptcy judges can enter final orders, and "non-core" proceedings that are subject to district court de novo review. *See* 28 U.S.C. §157(b). Congress expressly identified certain core proceedings, including "counterclaims by the estate against persons filing claims against the estate." §157(b)(2)(C). Despite Article III challenges, lower courts across the country have uniformly held for decades that bankruptcy courts can enter final orders on debtors' compulsory counterclaims to proofs of claim.[1] Until now.

The Ninth Circuit opinion here holds that under *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982) (*Marathon*) and *Katchen v. Landy*, 382 U.S. 323 (1966), core jurisdiction constitutionally exists under §157(b)(2)(C) only for compulsory counterclaims entirely encompassed within the allowance or disallowance of the creditor's claim against the estate and that raise no issue beyond that claim. Even though here the debtor's compulsory counterclaim constituted an affirmative defense to

[1] A debtor's compulsory counterclaim to a proof of claim is any counterclaim that, at the time of pleading, arises out of the same transaction or occurrence as the creditor's claim against the estate and is not already pending in another action. Fed. R. Bankr. P. 7013; Fed. R. Civ. P. 13(a).

QUESTIONS PRESENTED – Continued

the proof of claim and, if decided first, would have defeated it entirely, the Court held the counterclaim was non-core because the debtor had to prove additional elements to prevail on it.

Accordingly, the questions presented are:

1. Whether the Ninth Circuit opinion, which renders §157(b)(2)(C) surplusage in light of §157(b)(2)(B), contravenes Congress' intent in enacting §157(b)(2)(C).

2. Whether Congress may, under Articles I and III, constitutionally authorize core jurisdiction over debtors' compulsory counterclaims to proofs of claim.

3. Whether the Ninth Circuit misapplied *Marathon* and *Katchen* and contravened this Court's post-*Marathon* precedent, creating a circuit split in the process, by holding that Congress cannot constitutionally authorize non-Article III bankruptcy judges to enter final judgment on all compulsory counterclaims to proofs of claim.

4. Where, as here, a creditor dismisses a state court claim against a debtor, files a proof of that claim in the bankruptcy and litigates the claim against the estate in that forum, has the creditor consented to core jurisdiction over the debtor's compulsory counterclaim that encompasses an affirmative defense?

PARTIES TO THE PROCEEDING

The original parties to this case, Vickie Lynn Marshall ("Vickie") and Pierce Marshall ("Pierce"), died during the pendency of this appeal. The current parties are Howard K. Stern, Executor of the Estate of Vickie Lynn Marshall, and Elaine T. Marshall, Executrix of the Estate of E. Pierce Marshall.

For the sake of readability, we adopt the Ninth Circuit's approach and refer to the parties as Vickie and Pierce.

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PETITION FOR WRIT OF CERTIORARI

OPINIONS BELOW

The Ninth Circuit's opinion is reported at 600 F.3d 1037 (9th Cir. 2010), Appendix to the Petition ("App.") 1-89.

Three opinions of the District Court for the Central District of California are reported at 275 B.R. 5 (C.D. Cal. 2002), App. 90-214; 271 B.R. 858 (C.D. Cal. 2001), App. 217-34; and 264 B.R. 609 (C.D. Cal. 2001), App. 239-86. A fourth is unpublished, App. 235-38.

Two opinions of the Bankruptcy Court for the Central District of California are reported at 257 B.R. 35 (Bankr. C.D. Cal. 2000), App. 286-99; and 253 B.R. 550 (Bankr. C.D. Cal. 2000), App. 313-36. A third is unpublished, App. 305-12.

♦

JURISDICTION

The Ninth Circuit issued its opinion on March 19, 2010; it denied panel and *en banc* rehearing on May 5, 2010. App. 1, 337-38.

This Court has jurisdiction under 28 U.S.C. §1254(1). Jurisdiction was proper in the District Court under 28 U.S.C. §§1331 and 1334, and in the Ninth Circuit under 28 U.S.C. §1291.

♦

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

Relevant portions of Article I, §8, and the entirety of Article III of the United States Constitution are reprinted at App. 339-41.

28 U.S.C. §§157 ("§157"), 1331 and 1334 are reprinted at App. 342-47.

♦

STATEMENT OF THE CASE

Vickie's husband J. Howard Marshall, II ("Howard") attempted to provide for Vickie through an inter vivos trust. App. 25-26, 134-48, 198-202. However, his son Pierce suppressed or destroyed the trust instrument and stripped Howard of his assets before his death. App. 25-26, 143-202, 211-14. The bankruptcy and district courts found Pierce liable for tortious interference and awarded Vickie millions in compensatory and punitive damages. App. 3, 214.

The Bankruptcy Proceedings

In 1996, Vickie sought Chapter 11 bankruptcy protection following Howard's death. App. 91-93. Pierce dismissed a pending state-court defamation suit against Vickie and brought his defamation claims into the bankruptcy court via both a nondischargeability adversary complaint and a separate proof of claim for an unliquidated amount of damages. App. 14-16 nn.10 & 11, 77-87, 274-77; Supplemental

Excerpts of Record ("SER") 6101-02, 6801 (Pierce telling bankruptcy court that the amount of his creditor's claim "shall be determined by the adversary proceedings filed herein" and he's "happy" to litigate "[his] claim here" because "we did choose this forum").

Vickie objected to Pierce's proof of claim, answered his adversary complaint pleading truth as an affirmative defense, and filed a compulsory counterclaim for tortious interference with an inter vivos gift. App. 15-16, 48 n.29, 94, 378-81. This was the first time Vickie asserted that claim in any court. App. 48 n.29; *In re Marshall*, 273 B.R. 822, 825-26 (Bankr. C.D. Cal. 2002); SER 6757.

Shortly after Vickie filed her compulsory counterclaim, the bankruptcy court found it was core under subsections (B) and (C) of §157(b)(2). App. 294-96, 306-07. During trial in late 1999, the bankruptcy court summarily resolved Pierce's defamation claim against him on the grounds that Vickie did not publish or ratify the alleged defamatory statements. App. 18, 244-45. After trial, it found Pierce liable for tortious interference with a gift and awarded compensatory damages of $449 million (the amount of the intended trust) and $25 million in punitive damages, entering final judgment in December 2000. App. 18-20, 286-336. The court also found that Pierce engaged

in "massive discovery abuse," including destroying documents relevant to Vickie's claim. App. 320-26.[2]

The Texas Probate Proceedings

A Texas probate court began administering Howard's estate in August 1995. App. 11. Vickie first appeared in that proceeding in 1998, when she joined a pending will contest filed by Pierce's brother. App. 48 n.29. In January 2000, Vickie prophylactically filed her tortious interference with gift claim in the probate court after Pierce argued that the bankruptcy court lacked jurisdiction under the probate exception. App. 12, 48 n.29; *Marshall*, 273 B.R. at 825-26.

After the bankruptcy court entered judgment for Vickie in December 2000, Vickie immediately filed the bankruptcy judgment in the Texas probate court and voluntarily nonsuited her claims there without prejudice. App. 20, 232; *Marshall*, 273 B.R. at 826; SER 8426-27.

After nonsuiting her claims, Vickie remained in the probate proceedings only as a counterdefendant on a sanctions claim by Pierce. App. 21 & n.18, 223 n.4; SER 8427. Pierce then brought new claims against Vickie in an effort to re-litigate the issues the bankruptcy court had already decided. App. 21, 223

[2] The judgment was based, in part, on evidentiary sanctions. App. 19-20 n.17, 317 n.5.

n.4, 232; *Marshall*, 273 B.R. at 825-26; SER 8427-28, 8609-30.

Although the bankruptcy court directed Pierce to dismiss all his new probate claims, *Marshall*, 273 B.R. at 826, 831, Pierce's attorneys dismissed only a tortious interference claim, assuring the bankruptcy court that any risk of inconsistent judgments had been eliminated and that the "only" issue in the probate-court trial "directed at Ms. Marshall" was whether Howard and Vickie had an agreement for him to give her one-half his property, and that Pierce "only seek[s] to avoid any possibility of future litigation with Vickie Marshall over [Howard's estate] and to ensure that the Texas Probate Court can determine all claimants and efficiently administer that estate." SER 6624, 8470. The bankruptcy court found Pierce's claim "entirely consistent" with its judgment, which had "made no finding of an 'agreement' between [Vickie] and [Howard] to give her one-half of all his property." *Marshall*, 273 B.R. at 826-27, 831-32; SER 8585-86.

After her nonsuit, Vickie participated in the probate-court trial only as a counterdefendant. App. 21, 232. Pierce obtained a judgment against Vickie based on his "no agreement" theory, which became final in February 2002. App. 92; *Marshall*, 273 B.R. at 826-27, 831-32; SER 12260-61 & n.2.

The District Court Proceedings

Shortly after the bankruptcy court entered judgment and over a year before the Texas probate judgment became final, Pierce appealed the bankruptcy court judgment to the district court. App. 20, 96.

The district court concluded that Vickie's claim was a compulsory counterclaim to Pierce's defamation claim but was not a "core" proceeding because of post-pleading developments, *i.e.*, the amount that Vickie recovered on her counterclaim and the bankruptcy court's rationale in dismissing Pierce's claim. App. 236-38, 265-83. It treated the bankruptcy court's judgment as proposed and undertook a "comprehensive, complete and independent review of" the issues. App. 98, 284.

When Pierce subsequently moved for preclusion based on the Texas probate judgment, the district court denied preclusion because the requisite identity of issues was lacking and because Pierce's motion was untimely and inconsistent with fundamental fairness. App. 56 n.32, 223-33.

In March 2002, only one month after the Texas judgment became final, the district court affirmed the bankruptcy court's findings and entered judgment for Vickie. App. 91, 194-95, 215-16. It concluded Howard directed his lawyers to prepare an inter vivos trust for Vickie consisting of half the appreciation of his assets from the date of their marriage, App. 134-48, 198-202, but that Pierce conspired to suppress or

destroy the trust instrument and strip Howard of his assets, App. 145-202, 211-14.

It awarded compensatory damages of approximately $44.3 million and punitive damages of $44.3 million, finding "overwhelming" evidence of Pierce's "willfulness, maliciousness, and fraud." App. 26, 212, 214.

Ninth Circuit Appeal I

Pierce appealed and Vickie cross-appealed. App. 26-27. The Ninth Circuit reversed the judgment, concluding the probate exception to federal jurisdiction barred Vickie's counterclaim. *Id.*

In May 2006, this Court unanimously reversed and remanded to the Ninth Circuit for further proceedings to consider whether Vickie's claim was core and to address claim and issue preclusion. *Marshall v. Marshall*, 547 U.S. 293, 315 (2006).[3]

Ninth Circuit Appeal II

On March 19, 2010, nearly four years after remand, the Ninth Circuit again reversed the district court's judgment in favor of Vickie, holding her compulsory counterclaim was not a core proceeding

[3] Shortly after remand, Pierce died, and several months later, Vickie died; each were substituted on the appeal by their respective executors. App. 5-6 n.1.

under §157(b)(2)(C), and therefore the bankruptcy court's judgment was not "final," and the later Texas probate judgment should be given issue-preclusive effect. App. 55-57, 64-65.

In so concluding, the court made several key rulings:

- Vickie's counterclaim was a *compulsory* counterclaim to Pierce's proof of claim, "because the 'operative facts underlying [her] action' are the same as those underlying [Pierce's] defamation claim" and "[t]he defamation claim, [Vickie's] affirmative defense of truth, and her counterclaim for tortious interference all concern the alleged efforts by [Pierce] to obtain control of his father's estate" through improper means, App. 47-48 & n.29;

- Core jurisdiction can exist over counterclaims "based upon state law, not the Bankruptcy Code or something else that is unique to the bankruptcy context," and that "could have been brought in state court," App. 43-44 & nn.26, 27;

- The determination whether a counterclaim to a proof of claim is core under §157(b)(2)(C) "must focus largely on what is available to the court at the time of filing, that is, the parties' pleadings," App. 51-52;

- Vickie's success on her counterclaim would defeat Pierce's defamation claim

by establishing the affirmative defense of truth, App. 47-48, 55.

Although these rulings supported the conclusion that Vickie's counterclaim was core, the court – relying solely on *Katchen v. Landy*, 382 U.S. 323 (1966) and *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982) (*Marathon*) – narrowly construed §157(b)(2)(C) to mean that even a compulsory counterclaim to a proof of claim does not qualify as core *unless* it is "'so closely related to the proof of claim that the resolution of the counterclaim is necessary to resolve the allowance or disallowance of the claim itself.'" App. 50. It held Vickie's compulsory counterclaim was non-core because even if she proved through her counterclaim that the alleged defamatory statements were true, thus defeating Pierce's proof of claim, she would need to prove additional facts to prevail on her counterclaim, including damages; therefore, "its resolution was not a necessary precursor" to resolving Pierce's defamation claim against the estate and it "was not so closely related to his claim that they essentially merged, with her counterclaim becoming part and parcel of the bankruptcy court's claims determination and allowance process." App. 4, 49-50, 55.

To hold otherwise, the court concluded, would be "an expansive reading of § 157(b)(2)(C) [that] would certainly run afoul of the Court's holding in *Marathon*" and "arguably be inconsistent with the Congress' intent to revise the Bankruptcy Code in a

manner consistent with the principles of *Marathon* to make its jurisdictional grant constitutional." App. 46.

Because the conclusion that Vickie's counterclaim was non-core meant her bankruptcy judgment was not final, the court reversed the district court judgment on the basis of issue preclusion, finding the Texas probate court entered the earliest final judgment "on certain matters relevant to this proceeding." App. 4-5, 55-56, 64. It never addressed the district court's determination that binding her to the Texas court's findings would be fundamentally unfair. App. 56 n.32, 232.[4]

[4] Concurring in the result, Judge Kleinfeld identified "alternative" grounds for reversal that actually rested on assertions the majority *rejected* and the record *refutes*, App. 66:

- The concurrence states Pierce only sought a non-dischargeability determination, not damages from the bankruptcy estate. *Id.* The majority rejected that contention, App. 15-16 n.11, and the record disproves it, SER 6101-02, 6801, 8409-16.
- The concurrence couches Vickie's counterclaim as an "evasion of Pierce's constitutional right to jury trial in Texas." App. 66. But the majority correctly notes that Pierce *dismissed* his Texas defamation claim against Vickie after the bankruptcy filing. App. 14 n.10, 274-76.
- The concurrence asserts there wasn't even "related to" jurisdiction, because Vickie "had already been discharged and her creditors would get none of the money she sought from Pierce in her counterclaim." App. 66. The majority correctly concluded that the bankruptcy plan specified that

(Continued on following page)

Vickie petitioned for rehearing en banc on the grounds that the opinion erred in determining her counterclaim was non-core. App. 348-77. She also sought panel rehearing based on the panel's failure to determine whether the district court properly exercised its discretion to deny issue preclusion on fundamental fairness grounds. *Id.* The petition was denied. App. 337-38.

◆

REASONS TO GRANT THE PETITION

Purporting to follow *Marathon*, 458 U.S. 50, and *Katchen*, 382 U.S. 323, the Ninth Circuit has held that, even though §157(b)(2)(C) provides that bankruptcy courts may finally adjudicate "counterclaims by the estate against persons filing claims against the estate," Article III forecloses bankruptcy courts from finally adjudicating even a *compulsory*

the counterclaim proceeds be applied first to creditor claims. App. 17.

- The concurrence characterizes Pierce's defamation claim as a "personal injury" claim that §157(b)(5) makes non-core. App. 66, 74-76. It is doubtful that §157(b)(5) encompasses defamation (*e.g.*, *Massey Energy Co. v. W. Va. Consumers for Justice*, 351 B.R. 348, 351 (E.D. Va. 2006)) but in any event, §157(b)(5) is waived where, as here, the creditor files a proof of claim, alleges core jurisdiction and does not timely object to bankruptcy court adjudication (*In re Smith*, 389 B.R. 902, 910-16 (Bankr. D. Nev. 2008); *see* App. 266-67 n.17; SER 6023, 6101-02, 6801).

counterclaim to claims against the estate – unless the counterclaim's resolution is a "necessary precursor" to resolving the creditor's claim and "so closely related to [the] claim that they essentially merge[ ], with [the] counterclaim becoming part and parcel of the bankruptcy court's claims determination and allowance process." App. 51. Certiorari should be granted because the Ninth Circuit's ruling:

- Creates a circuit split and contravenes the decades-long practice of bankruptcy courts everywhere.
- Nullifies Congress' intent in enacting §157(b)(2)(C) – indeed, renders the statute superfluous.
- Is compelled by neither *Marathon*, which did not involve a counterclaim, nor *Katchen*, a non-Article III case involving the 1898 Bankruptcy Act – nor by the two read together.
- Ignores this Court's relevant post-*Marathon* authority, including *Commodity Futures Trading Commission v. Schor*, 478 U.S. 833 (1986) (*Schor*), which upheld the constitutionality of a statutory scheme permitting non-Article III judges to decide compulsory counterclaims.
- Ignores that Congress rectified *Marathon*'s separation-of-powers concerns, including making bankruptcy courts units of the district courts with their judges appointed by Article III judges.

- Creates the absurd requirement that debtors *must* file compulsory counterclaims in bankruptcy courts that cannot finally decide them.
- Effects a sea change in bankruptcy practice that will confound efficient bankruptcy administration by saddling courts with jurisdictional battles and splintering inextricably-linked claims between bankruptcy and district courts.

This Court should resolve this issue immediately: It is in the nature of bankruptcy practice that only a tiny fraction of cases reaches the circuit court level; thus, decades could pass before this Court has another opportunity to review this important issue.

I. THE OPINION UNDERMINES CONGRESS' INTENT IN ENACTING 28 U.S.C. §157(b)(2)(C), CREATING STATUTORY AND CONSTITUTIONAL QUESTIONS THAT ONLY THIS COURT CAN RESOLVE.

A. Backdrop To §157(b)(2)(C).

1. Before *Marathon*, the filing of a proof of claim generally authorized bankruptcy judges to determine compulsory counterclaims.

Before Congress enacted the bankruptcy act invalidated by *Marathon*, bankruptcy proceedings were either summary or plenary; bankruptcy judges tried summary actions, but plenary actions were litigated

in state or federal court. *In re Los Angeles Trust Deed & Mortgage Exch.*, 464 F.2d 1136, 1138-39 (9th Cir. 1972).

The federal circuits uniformly held that any creditor who filed a proof of claim in the bankruptcy had impliedly consented to summary jurisdiction over any compulsory counterclaim by the debtor or trustee. 1 Alan N. Resnick & Henry J. Sommer, Collier on Bankruptcy 3-32, ¶ 3.02[3][d][i] (16th ed. 2010). But they were split as to whether filing a proof of claim permitted the bankruptcy court to determine unrelated or permissive counterclaims. *Id.*; *compare Peters v. Lines*, 275 F.2d 919, 924-25 (9th Cir. 1960) *with Inter-State Nat'l Bank v. Luther*, 221 F.2d 382, 389-90 (10th Cir. 1955).

In 1966, this Court held in *Katchen* that the 1898 Bankruptcy Act conferred summary jurisdiction on the bankruptcy court to determine a trustee's counterclaim to recover a voidable preference, regardless whether the counterclaim arose from the same or a different transaction as the proof of claim. 382 U.S. at 325 & n.1. It held that the bankruptcy court could issue affirmative relief on the counterclaim because the creditor, by submitting a proof of claim, had subjected itself "'to all the consequences that attach to an appearance.'" *Katchen*, 382 U.S. at 335.

After *Katchen*, some commentators argued for summary jurisdiction over all debtor counterclaims. *See In re Depo*, 40 B.R. 537, 541-42 (N.D.N.Y. 1984) (citing authorities). Yet, most courts held that a proof

of claim established the creditor's implied consent to summary jurisdiction over all compulsory counterclaims *plus* any permissive counterclaims directly related to allowance or disallowance of the creditor claim, such as voidable preferences. *See, e.g., id.*; *Los Angeles Trust*, 464 F.2d at 1138-39; *In re Carnell Constr. Corp.*, 424 F.2d 296, 298-99 (3d Cir. 1970).

2. *Marathon* (a non-counterclaim case).

In 1978, Congress broadened the jurisdiction of bankruptcy judges by eliminating the summary/plenary distinction and conferring bankruptcy court jurisdiction over all proceedings arising under the Bankruptcy Code or arising in or related to bankruptcy cases. *Marathon*, 458 U.S. at 54.

In its splintered 1982 *Marathon* decision, this Court held it was unconstitutional for a non-Article III bankruptcy judge to determine a claim that was merely "related to" the bankruptcy case – in that case, a state law breach of contract action the debtor commenced against non-creditor Marathon, which had not filed a proof of claim or otherwise previously appeared in the bankruptcy case. *Id.* at 75, 86 (plurality), 89-91 (Rehnquist, J., concurring), 92 (Burger, J., dissenting).

The Court never addressed whether a non-Article III bankruptcy judge could determine debtor counterclaims to a proof of claim. The three-justice dissent, citing *Katchen*, noted that had Marathon filed a claim against the estate, the bankruptcy court

properly could have adjudicated the debtor's state-law claim as a counterclaim. 458 U.S. at 99-100 (White, J., dissenting). But in a footnote response, the plurality noted that *Katchen* neither discussed Article III nor involved the 1978 Act. 458 U.S. at 79 n.31.

The *Marathon* plurality's Article III concerns were partly based on the political branches' potential encroachment on the judiciary's powers. *See* 458 U.S. at 57-60, 64 n.15, 74, 83-84. Under the 1978 Act, the political branches appointed the bankruptcy judges and bankruptcy courts were independent of, and required to exercise all jurisdiction conferred on, the district courts. *Id.* at 79 n.31, 84-87.

B. In Enacting §157(b)(2)(C), Congress Intended Bankruptcy Courts To Have Core Jurisdiction Over Debtors' Compulsory Counterclaims To Proofs Of Claim.

Congress enacted the 1984 Bankruptcy Act "for the specific purpose of curing the constitutional problems of the scheme under which [*Marathon*] arose." *In re Mankin*, 823 F.2d 1296, 1306 (9th Cir. 1987). Among the changes: (1) bankruptcy courts are now units of the district courts, 28 U.S.C. §151; (2) Article III judges appoint the bankruptcy judges, 28 U.S.C. §152; and (3) district courts have discretion to delegate matters to bankruptcy courts and the power to withdraw referred matters, 28 U.S.C. §§1334(a), (b), 157(a), (d).

Congress also divided bankruptcy court jurisdiction into "core" proceedings that the bankruptcy court could finally adjudicate and "non-core" proceedings subject to district court de novo review. §157(b)(1), (3), (c)(1)-(2). Congress recognized *Marathon*'s narrow scope:

> *Marathon* was concerned with a very limited kind of proceeding. . . . It was not concerned even with all bankruptcy proceedings involving questions of State law in some way. It was concerned only with State law issues that did not arise in the core bankruptcy function of adjusting debtor-creditor rights.

130 Cong. Rec. 6242 (daily ed. March 21, 1984) (§157's co-sponsor Representative Kindness); 130 Cong. Rec. 6046-47 (daily ed. March 20, 1984) (co-sponsor Kastenmeier acknowledging constitutionality of bankruptcy jurisdiction by consent and describing *Katchen* as recognizing "that State common law actions become transformed into Federal bankruptcy matters when brought in proceedings integral to a bankruptcy case").

In accordance with its view of *Marathon*, Congress broadly defined core proceedings as those "arising under" the bankruptcy code and "arising in" bankruptcy cases, and specified in §157(b)(2) a non-exhaustive list of "various types of proceedings deemed by Congress to be core proceedings." *Mankin*, 823 F.2d at 1299-1300. Congress "'realized that the bankruptcy court's jurisdictional reach was essential to the efficient administration of bankruptcy proceedings

and intended that the 'core' jurisdiction would be construed as broadly as possible subject to the constitutional limits established in *Marathon*.'" *In re CBI Holding Co.*, 529 F.3d 432, 459-60 (2d Cir. 2008). It believed that *almost all proceedings* before bankruptcy judges – the sponsors said 95% – would be core. *In re Arnold Print Works, Inc.*, 815 F.2d 165, 168-69 (1st Cir. 1987) (Breyer, J.); *Mankin*, 823 F.2d at 1301; *see also* 130 Cong. Rec. 6045 (Kastenmeier stating core jurisdiction is "broader than the summary jurisdiction of the bankruptcy courts under pre-1978 law").

By specifying in §157(b)(2)(C) that "counterclaims by the estate against persons filing claims against the estate" are core proceedings, Congress sought to streamline bankruptcy administration while accommodating *Marathon* by providing that bankruptcy courts could enter final orders on such counterclaims. Congress understood that while bankruptcy courts would have "related to" (non-core) jurisdiction over non-bankruptcy-specific claims against persons who had not filed proofs of claim (the *Marathon* context), core jurisdiction would exist over counterclaims to proofs of claim that, by definition, concern the adjustment of debtor-creditor relations. *See* 130 Cong. Rec. 6046-47; *Marathon*, 458 U.S. at 71 (distinguishing "the restructuring of debtor-creditor relations, which

is at the core of the federal bankruptcy power" from the claim at issue).[5]

Unlike the debtor's claim against the non-creditor in *Marathon*, a debtor's counterclaim to a proof of claim "arises in" the bankruptcy case because the claims allowance process only exists in bankruptcy. *In re Bar M Petroleum Co.*, 63 B.R. 343, 346 (Bankr. W.D. Tex. 1986). A compulsory counterclaim, in particular, necessarily "arises in" the bankruptcy case because the debtor *must* file it in the bankruptcy case; if the debtor fails to assert it and the creditor's claim is successful, res judicata bars its subsequent assertion. 10 Alan N. Resnick & Henry J. Sommer, Collier on Bankruptcy ¶ 7013.02 (15th ed. 2008).

"By specifically including as core proceedings counterclaims brought by a debtor as a result of claims filed by creditors against the estate, Congress apparently believed that it is more efficient having a single court decide all cases based on the same facts and circumstances." *In re Fang Operators*, 158 B.R. 643, 647 (Bankr. N.D. Tex. 1993). Congress

[5] Judiciary-created emergency bankruptcy rules enacted in *Marathon*'s wake similarly prohibited bankruptcy courts from entering final judgments in "related proceedings," which included "claims brought by the estate against parties *who have not filed claims against the estate*" and did "*not* include . . . counterclaims by the estate in whatever amount against persons filing claims against the estate." 1 Collier on Bankruptcy, *supra* at 3-96 to 3-97 n.15, ¶ 3.10[2][b] (emphasis added).

Significantly, §157's sponsors intended to codify those emergency rules. *Id.* at 3-99; 130 Cong. Rec. 6045, 6242-44.

enacted the 1984 Act "to reduce substantially the time-consuming and expensive litigation regarding a bankruptcy court's jurisdiction over a particular proceeding" and to ensure "the efficient and expeditious resolution of all matters connected to the bankruptcy estate." *In re Fietz*, 852 F.2d 455, 457 (9th Cir. 1988).

C. The Opinion's Construction Of §157(b)(2)(C) Nullifies The Entire Provision.

The opinion recognizes that courts should avoid construing statutes "'in a manner that is strained and, at the same time, would render a statutory term superfluous.'" App. 43. It applies that rule to reject Pierce's contention that Vickie's counterclaim is non-core because it could have been brought in state court and is not bankruptcy-specific, reasoning "[w]e do not believe that Congress intended § 157(b)(2)(C) to be a meaningless (or near meaningless) provision, which is what it would become under Pierce Marshall's overly restrictive approach." App. 43-44.

Perversely, however, the opinion's core jurisdiction test itself renders §157(b)(2)(C) meaningless. By prohibiting core jurisdiction over a compulsory counterclaim unless it is necessary to determine the allowance or disallowance of the creditor claim and raises no issues outside that claim, the opinion makes §157(b)(2)(C) entirely superfluous, because Congress already specified in §157(b)(2)(B) that core proceedings include the "allowance or disallowance of claims

against the estate." If Congress had intended to limit core counterclaim jurisdiction to the allowance/disallowance of creditor claims, as the opinion holds, the counterclaim provision would have been unnecessary.

As this Court recognized in *Schor*, rejecting a circuit court's similar effort to straight-jacket a counterclaim statute under *Marathon*, the canon that courts should construe statutes to avoid constitutional questions "does not give a court the prerogative to ignore the legislative will in order to avoid constitutional adjudication." 478 U.S. at 841. The Ninth Circuit's narrow core jurisdiction test contravenes Congress' intent. Whether Article III compels that nullification is a question for this Court. Determining whether Congress exceeded its constitutional authority is "'a delicate exercise in constitutional interpretation, and is a responsibility of this Court as ultimate interpreter of the Constitution.'" *Marathon*, 458 U.S. at 62.

II. THE OPINION CREATES A CIRCUIT SPLIT AND CONTRAVENES THE DECADES-LONG PRACTICE OF COURTS NATIONWIDE.

A. The Opinion Creates A Circuit Split.

The opinion's narrow construction of §157(b)(2)(C) creates a circuit split. It is the only circuit decision in the three decades since the statute's enactment to ever find a compulsory counterclaim to a proof of claim to be non-core.

In *In re CBI Holding Co.*, for example, the Second Circuit considered a case where the debtor's auditor filed a proof of claim for $210,000 in unpaid pre-petition services for a 1994 audit, and the debtor's successor responded with compulsory contract and tort counterclaims, claiming the creditor committed $70 million in malpractice damages from 1992 through 1994. 529 F.3d at 355, 438, 441-42. The alleged malpractice was a defense to the creditor's claim, but the counterclaims also sought millions in malpractice damages relating to different years than those underlying the proof of claim. *Id.* at 461-62. In holding the counterclaims core, the Second Circuit recognized that *Marathon* merely held that "a non-Article III bankruptcy judge could not adjudicate a pre-petition contract dispute arising under state law against a party that had not filed a proof of claim and was not otherwise related to the bankruptcy proceedings." *Id.* at 459. It further recognized that nothing in *Marathon* "'alters the basic principle that the filing of a proof of claim invokes the special rules of bankruptcy,'" and thus counterclaims that are factually and legally connected to a proof of claim are core proceedings – regardless whether they rest on state law, could have existed independently of the bankruptcy, are disproportionate to the creditor's claim or involve issues that are not a defense to the creditor's claim. *Id.* at 461-65 & n.12. Thus, in *CBI*, the counterclaims went beyond mere allowance/disallowance of the creditor's claim – the boundary under the Ninth Circuit opinion.

Moreover, the First Circuit, citing *CBI* in support, has held that compulsory counterclaims to proofs of claim fall within §157(b)(2)'s definition of core proceedings. *In re Am. Bridge Prods.*, 599 F.3d 1, 4 (1st Cir. 2010). In that case, it upheld a bankruptcy court's authority to adjudicate the trustee's counterclaims seeking damages for negligence and breach of fiduciary duty against a receiver who filed a compensation claim. *Id.* at 2, 4.

Every other circuit decision involving a compulsory counterclaim to a proof of claim – decisions by the Third, Fifth and Sixth circuits – has found core jurisdiction even though the counterclaim went beyond mere allowance or disallowance of the proof of claim. *In re Baudoin*, 981 F.2d 736, 741-43 (5th Cir. 1993) (holding, for res judicata purposes, that debtor's lender liability claim should have been brought as core compulsory counterclaim to lender's proof of claim given common nucleus of operative facts); *In re MacLeod Co., Inc.*, 935 F.2d 270, 1991 WL 96718, *4 (6th Cir. 1991) (table) (upholding damage award to debtor on counterclaim for breach of contract);[6] *In re Meyertech Corp.*, 831 F.2d 410, 418 n.9 (3d Cir. 1987) (upholding open account damages to debtor exceeding creditor's breach-of-warranty damages).

[6] Unpublished Sixth Circuit decisions are not precedentially binding but may be considered for persuasive value. *United States v. Sanford*, 476 F.3d 391, 396 (6th Cir. 2007).

B. The Opinion Fundamentally Changes Bankruptcy Law Within The Ninth Circuit And Contravenes The Decades-Long Practice Of Courts Across The Country.

The opinion doesn't just create a circuit split. It fundamentally changes bankruptcy law as applied for decades by bankruptcy and district courts.

Courts within the Ninth Circuit have uniformly held that bankruptcy courts have core jurisdiction over debtors' compulsory counterclaims to proofs of claim. *See In re Gorilla Cos.*, 429 B.R. 308, 310, 313 (Bankr. D. Ariz. 2010) (noting "*Marshall* changed the law" and *Marshall* never addresses the Ninth Circuit's own precedent in *Peters*, 275 F.2d at 925, that filing a proof of claim constitutes consent to the bankruptcy court determining trustee counterclaims arising out of the same transaction); *In re PNP Holdings Corp.*, 184 B.R. 805, 806 (B.A.P. 9th Cir. 1995), *aff'd*, 99 F.3d 910 (9th Cir. 1996) ("[i]t is well settled that a creditor consents to jurisdiction over related counterclaims by filing a proof of claim"); *In re Lion Country Safari, Inc.*, 124 B.R. 566, 569 (Bankr. C.D. Cal. 1991); *In re County of Orange*, 203 B.R. 977, 980 (Bankr. C.D. Cal. 1996); *In re Marshland Dev.*, 129 B.R. 626, 631 n.10 (Bankr. N.D. Cal. 1991); *In re Beugen*, 81 B.R. 994, 1000 (Bankr. N.D. Cal. 1988); *In re Sun West Distribs.*, 69 B.R. 861, 863-64 (Bankr. S.D. Cal. 1987).

That also has been the decades-long view of bankruptcy and district courts everywhere. *See, e.g.*:

First Circuit: *In re Am. Bridge Prods.*, 398 B.R. 724, 729-30 (D. Mass. 2009), *vacated on other grounds*, 599 F.3d 1 (1st Cir. 2010); *In re Envisionet Computer Servs.*, 276 B.R. 7, 11 (D. Me. 2002); *In re Cont'l Fin. Res.*, 149 B.R. 260, 262-63 (Bankr. D. Mass. 1993), *aff'd*, 154 B.R. 385 (D. Mass 1993); *In re BKW Sys.*, 66 B.R. 546, 547-48 (Bankr. D. N.H. 1986); *Bedford Computer Corp. v. Ginn Publ'ns*, 63 B.R. 79, 81-83 (D. N.H. 1986).

Second Circuit: *In re S.W. Bach & Co.*, 425 B.R. 78, 90 (Bankr. S.D.N.Y. 2010); *In re G.M. Crocetti, Inc.*, 2008 WL 4601278, *3-*4 (S.D.N.Y. 2008); *In re Northwest Airlines Corp.*, 384 B.R. 51, 58 (S.D.N.Y. 2008); *In re Enron Corp.*, 349 B.R. 108, 112-13 (Bankr. S.D.N.Y. 2006); *In re CBI Holding Co.*, 311 B.R. 350, 362-63 (S.D.N.Y. 2004), *aff'd in part, rev'd in part on other grounds*, 529 F.3d 432, 459-64 (2d Cir. 2008); *In re Iridium Operating*, 285 B.R. 822, 831-32 (S.D.N.Y 2002); *In re Caldor, Inc.-NY*, 217 B.R. 121, 128 (Bankr. S.D.N.Y. 1998); *In re Paige*, 106 B.R. 346, 347 (Bankr. D. Conn. 1989); *In re Wiener Pharmaceuticals, Inc.*, 1988 Bankr. LEXIS 1097, *10-*16 (Bankr. E.D.N.Y. 1988); *In re STN Enters.*, 73 B.R. 470, 483-84 (Bankr. D. Vt. 1987); *In re Lombard-Wall, Inc.*, 48 B.R. 986, 990-91 (S.D.N.Y. 1985).

Third Circuit: *In re Asousa P'ship*, 276 B.R. 55, 66-72 (Bankr. E.D. Pa. 2002); *In re Milbourne*, 108

B.R. 522, 530 (Bankr. E.D. Pa. 1989); *Matter of L.B. Trucking, Inc.*, 75 B.R. 88, 91-92 (Bankr. D. Del. 1987).

Fourth Circuit: *Blackshire v. Litton Loan Servicing, L.P.*, 2009 WL 426130, *3 (S.D. W. Va. 2009); *In re Mercer's Enters.*, 387 B.R. 681, 686 (Bankr. E.D.N.C. 2008); *In re Doctors Health, Inc.*, 335 B.R. 95, 101 (Bankr. D. Md. 2005).

Fifth Circuit: *In re Gunsmiths, Inc.*, 271 B.R. 487, 490-91 (S.D. Miss. 2000); *In re Efficient Solutions, Inc.*, 2000 WL 1876356, *6 (E.D. La. 2000); *Allen v. City Fin. Co.*, 224 B.R. 347, 352 (S.D. Miss. 1998); *Fang Operators*, 158 B.R. at 647-48; *Bar M*, 63 B.R. at 346-48.

Sixth Circuit: *In re Federated Dep't Stores, Inc.*, 240 B.R. 711, 722 (Bankr. S.D. Ohio 1999); *In re Nationwide Roofing & Sheet Metal*, 130 B.R. 768, 776 (Bankr. S.D. Ohio 1991).

Seventh Circuit: *In re K & R Express Sys., Inc.*, 382 B.R. 443, 447 (N.D. Ill. 2007); *In re ABC-Naco, Inc.*, 294 B.R. 832, 837 (Bankr. N.D. Ill. 2003); *In re Chapman*, 154 B.R. 258, 261 (Bankr. N.D. Ill. 1993).

Eighth Circuit: *In re SRC Holdings Corp.*, 352 B.R. 103, 165 (Bankr. D. Minn. 2006), *rev'd on other grounds*, *Leonard v. Dorsey & Whitney LLP*, 553 F.3d 609 (8th Cir. 2009); *In re Aerni*, 86 B.R. 203, 206-08 (Bankr. D. Neb. 1988); *In re Yagow*, 53 B.R. 737, 740 (Bankr. D. N.D. 1985).

Tenth Circuit: *In re C.W. Mining Co.*, 2009 WL 4906702, *3 (D. Utah 2009); *In re Geneva Steel, LLC*, 343 B.R. 273, 277-78 (Bankr. D. Utah 2006); *In re Applied Thermal Sys., Inc.*, 294 B.R. 784, 787-89 (Bankr. N.D. Okla. 2003); *In re Bokum Res. Corp.*, 64 B.R. 924, 928-30 (Bankr. D. N.M. 1986).

Eleventh Circuit: *In re Norrell*, 198 B.R. 987, 994 n.4 (Bankr. N.D. Ala. 1996); *In re I.A. Durbin, Inc.*, 62 B.R. 139, 143 (S.D. Fla. 1986); *In re Macon Prestressed Concrete*, 46 B.R. 727, 730 (M.D. Ga. 1985).[7]

C. The Opinion Exacerbates Confusion Over *Marathon* By Announcing A Standard No Other Court Has Embraced.

On the other side of this mountain of authority lie a handful of decisions from the mid-1980's that proffer an outdated view of *Marathon*. For example, in stating it is "unsettled" and "unclear" as to whether core jurisdiction exists over counterclaims arising out of the same transaction as the creditor claim, the Collier bankruptcy treatise cites three circuit court decisions for the view that core jurisdiction exists (1 Collier on Bankruptcy, *supra* at 3-33 n.49, 3-34, ¶ 3.02[3][d], citing *CBI*, *Baudoin* and *Meyertech*), but cites only two 1985 bankruptcy court decisions for

[7] Although no published D.C Circuit case directly addresses the issue, dicta supports the prevailing view that core jurisdiction exists. *See In re Auto-Pak, Inc.*, 52 B.R. 3, 4-5 (Bankr. D.C. Cir. 1985).

the view that some compulsory counterclaims might be non-core (1 Collier on Bankruptcy, *supra* at 3-33 n.51, ¶ 3.02[3][d], citing *In re Nanodata Computer Corp.*, 52 B.R. 334 (Bankr. W.D.N.Y. 1985), *aff'd on other grounds*, 74 B.R. 766 (W.D.N.Y. 1987) and *In re Illinois-California Express, Inc.*, 50 B.R. 232 (Bankr. D. Colo. 1985)).

Those two 1985 bankruptcy court decisions, both decided before *Schor*, broadly construed *Marathon* as requiring an Article III judge to decide all routine state law claims, including those asserted as counterclaims. *See* 1 Collier on Bankruptcy, *supra* at 3-33 to 3-34, ¶ 3.02[3][d]; *Nanodata*, 52 B.R. at 342; *Illinois-California Express*, 50 B.R. at 239. Their view of *Marathon* has been criticized as unsound and inconsistent with this Court's post-*Marathon* decisions. *See, e.g.*, *Crocetti*, 2008 WL 4601278 at *5; *Fang Operators*, 158 B.R. at 647; *In re Kaiser Steel Corp.*, 95 B.R. 782, 786-87 (Bankr. D. Colo. 1989); *Wiener Pharmaceuticals*, 1988 Bankr. LEXIS 1097, at *11-*14; *STN*, 73 B.R. at 483-84; *Bokum*, 64 B.R. at 928; *Durbin*, 62 B.R. at 141-43; *Bar M*, 63 B.R. at 346-48. Not only does their view contravene the settled rule "that merely because a claim involves consideration of state law issues, it does not mean that a bankruptcy court cannot consider such issues" (*Fang Operators*, 158 B.R. at 647), it contravenes this Court's subsequent decisions, such as *Schor* and *Thomas v. Union Carbide Agricultural Products Co.*, 473 U.S. 568 (1985), which "narrow the scope and impact of *Marathon* and confirm the concept of jurisdiction by

consent" (*Bokum*, 64 B.R. at 928; *accord*, *Kaiser Steel*, 95 B.R. at 786-87). Indeed, *Nanodata* relied on the circuit decision this Court reversed in *Schor*. *See* 52 B.R. at 343 n.32.

The Ninth Circuit opinion, by holding that the state law predicate for Vickie's compulsory counterclaim does not render it non-core, joins the modern chorus rejecting the outdated view of *Marathon* espoused in *Nanodata* and *Illinois-California Express*. Unfortunately, it adds a new layer of confusion by announcing a core jurisdiction test for compulsory counterclaims that no other court has adopted in the three decades since *Marathon*.

III. THE OPINION MISAPPLIES *MARATHON* AND *KATCHEN*, WHILE IGNORING THIS COURT'S POST-*MARATHON* PRECEDENT.

This Court's review is particularly warranted because the circuit split arises from confusion over this Court's decisions. This Court has acknowledged problems inherent in its Article III precedents. *Schor*, 478 U.S. at 847 ("our precedents in this area do not admit of easy synthesis"); *Thomas*, 473 U.S. at 583 ("[a]n absolute construction of Article III is not possible in this area of 'frequently arcane distinctions and confusing precedents'").

The uncertainty is magnified in the debtor-counterclaim context because this Court has never addressed §157(b)(2)(C), and its only bankruptcy-counterclaim decisions (*e.g.*, *Katchen*, *Langenkamp v.*

Culp, 498 U.S. 42 (1990)) have involved avoiding powers such as preferences or voidable transfers – a context where "[i]t is a simple matter to conclude that . . . core treatment should be afforded the counterclaim," since "the creditor's claim cannot be allowed unless the property received by the creditor or its value has been returned." 1 Collier on Bankruptcy, *supra* at 3-33, ¶ 3.02[3][d]. "When the counterclaim asserted is not based upon the avoiding powers, but instead is either compulsory or permissive, the considerations become more complex." *Id.*

A. *Katchen*.

The Ninth Circuit opinion states, without explication of rationale, that its "construction of §157(b)(2)(C) . . . follows *Katchen*." App. 50.

However, *Katchen* was not an Article III case and it involved a statutory construction issue peculiar to the 1898 Bankruptcy Act. Although Congress had not expressly conferred summary jurisdiction on bankruptcy referees to order claimants to surrender preferences, this Court concluded that the trustee's preference counterclaim fell within the bankruptcy referee's express statutory power over the allowance/disallowance of creditor claims, because the creditor claim depended on whether the creditor received a voidable preference and the counterclaim therefore was part and parcel of the claims allowance process. *Katchen*, 382 U.S. at 328-35. It held that its statutory interpretation did not violate the right to jury trial,

because issues that arise in the claims allowance process are triable in equity. *Id.* at 335-40.

As one court recently recognized, the Ninth Circuit's reliance on *Katchen* to narrow core jurisdiction over compulsory counterclaims is puzzling, because *Katchen* did not abrogate the then-prevailing view that a bankruptcy court's summary jurisdiction included compulsory counterclaims; rather, *Katchen* held summary jurisdiction extended to preference counterclaims even if permissive, *i.e.*, those "unrelated to the transaction in which the creditor had received a preference." *Gorilla Cos.*, 429 B.R. at 312; *see Katchen*, 382 U.S. at 325-26 & n.1.

Other courts have construed *Katchen* as supporting bankruptcy court power to decide compulsory counterclaims, both before §157(b)(2)(C)'s enactment (*see* §I.A.1, *supra*) and after (*e.g.*, *Applied Thermal Systems*, 294 B.R. at 787-88; *Beugen*, 81 B.R. at 998-99; 2 Hon. William H. Brown, The Law of Debtors and Creditors §11:11, 11-41 (2010) [*Katchen* "has generally been broadly read to stand for the proposition that a creditor, by filing proof of claim, has consented to the jurisdiction of the bankruptcy court to grant an affirmative judgment against the claimant"]).

Only review by this Court can resolve the confusion. 1 Collier on Bankruptcy, *supra* at 3-34, ¶ 3.02[3][d] ("[u]ntil the Supreme Court sees fit specifically to disavow the *Katchen* rationale," it "seems that" counterclaims based on avoiding powers should

be core, counterclaims arising out of a different transaction should be non-core, and it "is unclear" whether counterclaims arising out of the same transaction are core).

B. *Marathon*.

Although the Ninth Circuit opinion states that *Marathon* compels its construction of §157(b)(2)(C), it never attempts to explain why. App. 49-50.

It couldn't even if it tried. This Court's fractured *Marathon* decision held only that it was unconstitutional for a bankruptcy court to determine a debtor's pre-petition state law claim against a defendant that was dragged into the bankruptcy case *involuntarily*, because it had not filed a proof of claim or otherwise previously appeared in the case. *CBI*, 529 F.3d at 459; *In re SG Philips Constructors, Inc.*, 45 F.3d 702, 706 (2d Cir. 1995) (the *Marathon* defendant was "involuntarily subjected to having the debtor's state law claim against it decided by an Article I judge" because it "had not filed a proof of claim and had no other connection with the bankruptcy").

The *Marathon* plurality's Article III concerns were clear in the context of a non-Article III judge appointed by the political branches determining claims against someone dragged into the bankruptcy. But the Ninth Circuit opinion fails to explain why those concerns would apply to a creditor who files a proof of claim under today's very different bankruptcy scheme controlled by Article III judges.

C. *Thomas/Schor.*

The Opinion also ignores this Court's subsequent decisions limiting *Marathon*'s scope and impact.

In 1985, this Court acknowledged that the justices could not agree on Article III's scope in *Marathon* and that *Marathon* only establishes that a non-Article III court cannot render final judgment "in a traditional contract action arising under state law, *without consent of the litigants*, and subject only to ordinary appellate review." *Thomas*, 473 U.S. at 584 (emphasis added). The Court advised that "practical attention to substance rather than doctrinaire reliance on formal categories should inform application of Article III" and that courts must consider the "concerns guiding the selection by Congress of a particular method for resolving disputes" when "assessing the degree of judicial involvement required by Article III." *Id.* at 587.

A year later, in *Schor*, it rejected an Article III challenge to a statutory scheme that allowed customers to sue their commodity brokers before non-Article III commissioners, the Commodity Futures Trading Commission (CFTC), and allowed the CFTC, in conformance with Congress' goal of efficient dispute resolution, to adjudicate counterclaims "'aris[ing] out of the transaction or occurrence or series of transactions or occurrences set forth in the complaint.'" *Schor*, 478 U.S. at 837, 850. The subject counterclaim was a state-law claim normally reserved to Article III courts, and the customer who filed the CFTC claim

objected to the counterclaim jurisdiction. *Id.* at 838-39, 853.

This Court rejected the Circuit Court's conclusion that *Marathon* made the statute unconstitutional. *Id.* at 839-40. It recognized that the right to adjudication of claims and counterclaims by an Article III judge is a personal right that can be impliedly waived by filing a claim in a non-Article III forum, and that the absence of such consent was a crucial factor in *Marathon*. *Id.* at 839-40, 848-49. It rejected "formalistic and unbending rules" that would "unduly constrict Congress' ability to take needed and innovative action pursuant to its Article I powers," and instead advised courts to give due regard in each case to the "practical consequences" of Congress' adjudicatory scheme "in light of the larger concerns that underlie Article III," concluding that the CFTC statute did not impermissibly intrude on the judiciary. *Id.* at 851, 857. In observing that the CFTC's jurisdiction was "not without precedent," it described *Katchen* as upholding "a bankruptcy referee's power to hear and decide state law counterclaims against a creditor who filed a claim in bankruptcy when those counterclaims arose out of the same transaction." *Schor*, 478 U.S. at 852.

Numerous courts have concluded that "a fair reading of *Schor* leads to the conclusion" that bankruptcy courts have core jurisdiction over debtor counterclaims arising out of the same transaction as the proof of claim. *Bokum*, 64 B.R. at 930; *accord Applied Thermal Sys.*, 294 B.R. at 787 n.8; *Beugen*, 81 B.R. at 1000; *STN*, 73 B.R. at 483; *Sun West*, 69 B.R. at 865;

see Kaiser Steel, 95 B.R. at 787 ("The holdings of *Schor* and *Thomas* in the bankruptcy setting had, in fact, been anticipated by Congress in the enactment of 28 U.S.C. §157(c)(2)").

They recognize that filing a proof of claim is sufficiently voluntary to constitute consent to compulsory counterclaims. *See, e.g., Applied Thermal Sys.*, 294 B.R. at 791 ("if [the creditor] was concerned about defending counterclaims in bankruptcy court, it should have foregone filing its proof of claim against the estate of [the debtor]"); *Lion Country Safari*, 124 B.R. at 572 ("The filing of a proof of claim by a creditor is 'voluntary' in the sense that a creditor is not required to file a proof of claim, and pursue it within the bankruptcy court"); *Wiener Pharmaceuticals*, 1988 Bankr. LEXIS 1097 at *16 ("To call it jurisdiction by ambush is simply to use pejorative terms for what is the well known consequence of filing a claim. The defendants here could have avoided the jurisdiction of the bankruptcy court by refraining from asserting a right to share in the distribution of the debtor's estate.").

Consistent with *Schor*'s pragmatic balancing approach, courts and commentators have also recognized that the 1984 Act's procedural changes – e.g., the appointment and dismissal of bankruptcy judges by Article III judges (instead of the political branches) and the district court's unfettered discretion to refer or withdraw jurisdiction – substantially diminish the threat of political-branch encroachment on the judiciary that undergirded much of the

Marathon plurality's concerns. *E.g.*, *Mankin*, 823 F.2d at 1309; *In re Finevest Foods, Inc.*, 143 B.R. 964, 967-71 (Bankr. M.D. Fla. 1992); *In re Jennings*, 83 B.R. 752, 760-61 (D. Nev. 1988); Troy A. McKenzie, *Judicial Independence, Autonomy, and the Bankruptcy Courts*, 62 Stan. L. Rev. 747, 793 (2010) ("[d]espite lacking the structural protections of tenure during good behavior and undiminished salary, bankruptcy judges are, perhaps counterintuitively, *more* insulated from the legislative and executive branches than most federal district judges"); *id.* at 806 ("[a] more full-bodied assessment of the bankruptcy courts suggests that the qualities of the bankruptcy bench and bar provide adequate substitutes for the qualities that courts and commentators reference when they invoke 'Article III values'").

Courts also have recognized that *Schor* and *Thomas* "turned to history and tradition to help define the type of adjudicatory proceeding that the Constitution reserves exclusively for Article III Courts." *Arnold Print Works*, 815 F.2d at 169 (Breyer, J.). A historical definition supports core jurisdiction over compulsory counterclaims, since "[c]ounterclaims arising from the same transaction as the creditor's claim have also been traditionally adjudicated by non-Article III bankruptcy judges." *Beugen*, 81 B.R. at 1000.

D. *Granfinanciera/Langenkamp.*

A few years after *Schor*, this Court rendered two bankruptcy decisions that confirm the constitutional importance of filing a proof of claim:

- *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33, 56-59 (1989) held that a defendant who had not filed a proof of claim had a right to jury trial on a trustee's fraudulent conveyance action, because the absence of a proof of claim made the trustee's right to recover a fraudulent conveyance a private right, rather than a counterclaim arising in the claims allowance process.

- A year later, *Langenkamp* held that creditors who filed proofs of claim had no right to jury trial on a trustee's preference counterclaim because the proofs of claim triggered the process of claims allowance/disallowance, bringing the creditor within the bankruptcy court's equitable jurisdiction. 498 U.S. at 44-45.

Cases and commentators have construed these decisions as supporting core jurisdiction over compulsory counterclaims. *E.g.*, *Fang Operators*, 158 B.R. at 646; *Asousa P'ship*, 276 B.R. at 67; Jonathan P. Friedland, Commercial Bankruptcy Litigation §3:27, 3-56 (2d ed. 2009) ("*Granfinanciera* and *Langenkamp* establish the constitutionality of the bankruptcy court's core jurisdiction over . . . counterclaims by the

estate against persons filing claims against the estate, designated core by section 157(b)(2)(C)").

Yet, *Granfinanciera* and *Langenkamp* only addressed trustee claims for fraudulent conveyance and preference. Thus, "[e]ach of the three Supreme Court cases speaking to the waiver effected by filing a proof of claim – *Katchen v. Landy*, *Granfinanciera* and *Langenkamp v. Culp* – involved avoiding power counterclaims. It is not surprising that the Court found the counterclaims to be part of the claims allowance process; a claim cannot be allowed if the claimant has not returned property conveyed by the debtor in an avoidable transaction. Whether the same is true of other types of counterclaims is less clear." 1 Collier on Bankruptcy, *supra* at 3-81 ¶ 3.08[2][a].

IV. THE COURT SHOULD RESOLVE THE CIRCUIT SPLIT IMMEDIATELY.

A. The Presented Issues Rarely Reach The Circuit Level.

The issues presented by this petition rarely reach the circuit level, as confirmed by the paucity of relevant circuit decisions in the three decades since §157(b)(2)(C)'s enactment. "The nature of bankruptcy cases tends to discourage further appellate review in the Article III courts because of the twin concerns of delay and cost associated with prolonged litigation." McKenzie, *supra*, 62 Stan. L. Rev. at 782. Between 2000 and 2007, the ratio between cases filed and the number of appeals was only one for every 1,580

bankruptcy cases, compared to one for every 12 civil cases. *Id.* at 783-84.

Moreover, not only do "[b]ankruptcy cases generate few appeals," but "the structure of appellate review in bankruptcy cases complicates the generation of binding precedent to guide the resolution of future disputes, and the Article III courts have little appetite for entertaining those appeals that do make it out of the bankruptcy courts." *Id.* at 751-52. Consequently, a gap often exists "between appellate decisionmaking and the law as applied in the bankruptcy courts. The disputes that generate reported opinions in bankruptcy cases tend not to be ordinary disputes involving somewhat unsettled areas of law. Rather, they tend to be decisions that are notable outliers, with resulting interpretations of the law that are . . . 'often out of sync with long-standing practice.'" *Id.* at 784. That aptly describes the opinion here – an outlier decision in an extraordinary case that alters long-standing practices.

Decades could pass before these important issues reach this Court again.

B. The Opinion Is Already Causing Confusion.

The prevailing view that core jurisdiction exists over all debtor compulsory counterclaims to proofs of claim rests on multiple analytical rationales:

- Since compulsory counterclaims arise from the same subject matter as the proof of claim, they relate to the core bankruptcy power of adjusting creditor-debtor relations and therefore adjudicate public rights. *Applied Thermal Sys.*, 294 B.R. at 789; *Beugen*, 81 B.R. at 1000; *Bar M*, 63 B.R. at 346-47.

- *Marathon* did not alter the rule that filing a proof of claim invokes the special rules of bankruptcy. *CBI*, 529 F.3d at 462.

- Creditors who file proofs of claim consent to the bankruptcy court adjudicating compulsory counterclaims. *Applied Thermal Sys.*, 294 B.R. at 788-89; *Asousa P'ship*, 276 B.R. at 66-67; *Beugen*, 81 B.R. at 1001; *STN*, 73 B.R. at 483; *Sun West*, 69 B.R. at 864-65; *Bokum*, 64 B.R. at 930.

- Because compulsory counterclaims arise from the same transaction as the creditor's claim against the estate, they "need no jurisdictional basis beyond [§157(b)(2)(C)] because the bankruptcy court's jurisdiction is ancillary to its jurisdiction over the creditor's claim." 9 Am. Jur. 2d Bankruptcy § 782 (2010); *accord*, *Lion Country Safari*, 124 B.R. at 569; *Yagow*, 53 B.R. at 740.

In stark contrast, the Ninth Circuit's opinion provides no such analytical moorings for its new core

jurisdiction test for compulsory counterclaims. As Bankruptcy Judge Randolph Haines recently explained in a detailed critique, the opinion's new test is difficult to decipher, let alone apply, because *Katchen* and *Marathon* – the two cases the opinion cites – did not find any constitutional problem with bankruptcy courts deciding compulsory counterclaims to proofs of claim, the opinion never clearly identifies what constitutional limits exist for such counterclaims, it never addresses the Ninth Circuit's own precedent concluding that filing a proof of claim constitutes consent to summary jurisdiction over compulsory counterclaims, and its test for non-core jurisdiction rests on imprecise guideposts, such as the nexus between the claim and counterclaim being "'somewhat attenuated'" or the claims not being sufficiently "'part and parcel'" of each other. *Gorilla Cos.*, 429 B.R. at 312-13. Unless this Court steps in, the opinion will wreak confusion among Ninth Circuit bankruptcy courts.

C. The Opinion Will Confound Bankruptcy Administration In An Area Where Nationwide Uniformity Is Crucial.

The opinion will flout Congress' goal of efficient and expeditious bankruptcy administration. *See* §I.B, *supra*. It splinters the determination of creditor claims against the estate and compulsory counterclaims into different forums. It produces the absurd result that debtors must file compulsory counterclaims in bankruptcy courts that cannot finally

adjudicate them. It will swamp bankruptcy and district courts with abstention and withdrawal motions. And by requiring district courts to determine compulsory counterclaims, which by definition are legally and factually interconnected to creditor claims being adjudged by the bankruptcy court, it will spawn endless litigation and confusion over jurisdictional limits and claim and issue preclusion – the exact opposite of what Congress intended.

If Article III truly compels this result, this Court should say so immediately so Congress can address the repercussions. And if, as petitioner submits, the opinion is simply wrong, this Court should say so immediately to prevent the jurisdictional and administrative complication that the opinion will engender. Moreover, the presence of a circuit split in this area is repugnant; bankruptcy is an area where the Constitution itself recognizes the importance of nationwide uniformity. U.S. Const. Art. I, §8 (granting Congress the power to establish "uniform Laws on the subject of Bankruptcies throughout the United States").

♦

CONCLUSION

For all the foregoing reasons, the petition for writ of certiorari should be granted.

Dated: August 3, 2010

Respectfully submitted,

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600 F.3d 1037 (9th Cir. 2010)

Volume 1 of 2

FOR PUBLICATION

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

In re: VICKIE LYNN MARSHALL,
Debtor.

ELAINE T. MARSHALL,
Executrix of the
Estate of E. Pierce Marshall,
Plaintiff-Counter-Defendant/
Appellant-Cross-Appellee,

v.

HOWARD K. STERN,
Executor of the
Estate of Vickie Lynn Marshall,
Defendant-Counter-Claimant/
Appellee-Cross-Appellant.

Nos. 02-56002,
02-56067

D.C. No.
CV-01-00097-DOC
Central District of
California, Santa Ana

OPINION

On Remand from the United States Supreme Court

Argued and Submitted
June 25, 2009 – Seattle, Washington

Filed March 19, 2010

Before: Robert R. Beezer, Andrew J. Kleinfeld and
Richard A. Paez, Circuit Judges.

Opinion by Judge Beezer;
Concurrence by Judge Kleinfeld

COUNSEL

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OPINION

BEEZER, Circuit Judge:

This case returns to us after the Supreme Court determined that we had construed too broadly the "probate exception" to our subject matter jurisdiction. *Marshall v. Marshall,* 547 U.S. 293 (2006). Confident that we have subject matter jurisdiction over this case, *id.*; 28 U.S.C. § 1291, we turn to the merits of the longstanding and acrimonious dispute.

This case involves a tort claim by Vickie Lynn Marshall against E. Pierce Marshall, the son of her late husband J. Howard Marshall II, for Pierce Marshall's purported interference with a substantial inter vivos gift (estimated to exceed $300 million) that her late husband intended to give to her. The claim comes to us in an unusual procedural posture. It was asserted as a state law counterclaim to a nondischargeability complaint and proof of claim that

Pierce Marshall filed in Vickie Lynn Marshall's bankruptcy proceedings in the Central District of California. Both the bankruptcy and district courts found that Pierce Marshall was liable for tortious interference and awarded Vickie Lynn Marshall millions of dollars in compensatory and punitive damages.

While Vickie Lynn Marshall's tortious interference claim was pending in federal court in California, a probate court in Texas was administering the estate of J. Howard Marshall II. Both Vickie Lynn Marshall and Pierce Marshall were actively engaged in this Texas litigation, participating fully in the five-month jury trial held by the Texas probate court. To discern J. Howard Marshall II's true intentions regarding his will and assets held in trust, the Texas probate court had to resolve allegations that J. Howard Marshall II's estate plan and the transactions underlying it were tainted by illegality and that, contrary to his estate plan, J. Howard Marshall II intended to give Vickie Lynn Marshall a substantial inter vivos gift. In its judgment, which was issued after the bankruptcy court's "judgment" on Vickie Lynn Marshall's tortious interference claim but before the district court had adjudicated the appeal from the bankruptcy court, the Texas probate court upheld the validity of J. Howard Marshall's estate plan and estate planning documents, finding that J. Howard knowingly effected his estate plan free from the undue influence or coercion of his son Pierce Marshall. The Texas probate court further

found that J. Howard Marshall II did not intend to give Vickie Lynn Marshall a gift from the assets that passed through his will or that were held in his living trust. These and other legal and factual determinations adverse to Vickie Lynn Marshall would be fatal to her tortious interference counterclaim, should they be afforded preclusive effect in this proceeding.

We conclude that the findings of the Texas probate court should be afforded preclusive effect because it is the earliest final judgment on matters relevant to this proceeding. The bankruptcy court exceeded its statutory grant of power and the constitutional limitations on that power when it purported to enter a final judgment in favor of Vickie Lynn Marshall on her counterclaim. The bankruptcy court is empowered by 28 U.S.C. § 157(b)(1) to hear and finally determine "core proceedings arising under title 11, or arising in a case under title 11." Vickie Lynn Marshall's counterclaim for tortious interference is not such a "core proceeding" because its resolution was not a necessary precursor to the resolution of Pierce Marshall's claim against the bankruptcy estate for defamation. In other words, her counterclaim was not so closely related to his claim that they essentially merged, with her counterclaim becoming part and parcel of the bankruptcy court's claims determination and allowance process. Thus, the bankruptcy court could, at most, enter proposed findings of fact and conclusions of law on Vickie Lynn Marshall's counterclaim for tortious interference. *See* 28 U.S.C. § 157(c).

The district court should have afforded preclusive effect to the Texas probate court's factual findings and relevant legal conclusions. The determinations adverse to Vickie Lynn Marshall in the Texas probate court prevent her from establishing the elements of her counterclaim, such as J. Howard Marshall II's intent to give her a substantial inter vivos gift, the tortious nature of Pierce Marshall's conduct regarding the estate planning documents, and the reasonableness and amount of her expectancy. We reverse the judgment of the district court and remand with instructions that judgment be entered in favor of the Estate of Pierce Marshall.

I

This case arises out of the bankruptcy of appellee/cross-appellant Vickie Lynn Marshall, the widow of the late J. Howard Marshall II. During the course of her bankruptcy, Vickie Lynn Marshall made a counterclaim for tortious interference with a gift expectancy against appellant/cross-appellee E. Pierce Marshall, the younger of J. Howard Marshall II's two sons, who had sought a determination of nondischargeability and filed a proof of claim against Vickie Lynn Marshall's bankruptcy estate.[1] Vickie Lynn

[1] Both of the original parties are now themselves deceased. Elaine T. Marshall is the executrix of Pierce Marshall's estate and has filed a notice of appearance in this court on behalf of his estate. Howard K. Stern is the executor of Vickie Lynn Marshall's estate and has filed a notice of appearance in this

(Continued on following page)

Marshall's counterclaim is the focus of this appeal. Although the case arises out of her bankruptcy, a broader review of the relationships between Vickie Lynn Marshall, J. Howard Marshall II, and Pierce Marshall, the business and estate planning measures of J. Howard Marshall II, and the Texas probate proceeding is necessary to appreciate the issues before us.

court on behalf of her estate. For the sake of readability, we refer to Vickie Lynn Marshall and Pierce Marshall in the present tense as if they are still living and are still the current parties.

Additionally, on March 19, 2009, we ordered the parties to "identify (1) all parties in interest, (2) the attorneys of record, (3) the real parties in interest, (4) any executors of an estate having an interest in these proceedings and (5) any guardian and/or guardian ad litem of an interested minor." Both parties filed responses to our order stating that the correct parties are currently before us. No third party has sought to intervene in this appeal.

The interests of Vickie Lynn Marshall's minor daughter, "DB," are represented by DB's father and legal guardian, Larry E. Birkhead, as determined by the Los Angeles Superior Court in *In re Vickie Lynn Marshall,* Case Nos. BP-104574, BP-104575. Mr. Birkhead had notice of these proceedings, attended oral argument, and at no time sought to intervene as a party on behalf of his daughter. Under California law, the executor or administrator of an estate is the real party in interest. *See Olson v. Toy,* 54 Cal. Rptr. 2d 29, 33 (Ct. App. 1996). Both parties here agreed that we did not need to appoint a guardian ad litem for DB, but that her interests in this proceeding were adequately represented by Mr. Birkhead and Mr. Stern. *See* Supplemental Opening Br. filed by Elaine Marshall at 58; Supplemental Answering Br. filed by Howard Stern at 66.

A

As detailed by the district court, J. Howard Marshall II was a self-made entrepreneur who eventually found great success in the oil industry. Born in 1905, J. Howard Marshall II attended Haverford College and graduated *magna cum laude* from Yale Law School before working during the 1930s for the Roosevelt Administration on the proration of oil production. After continued involvement in the oil industry, J. Howard Marshall II became one of the founders of the Great Northern Oil and Gas Company in 1954. The wealth of the Marshall family is primarily based on the interest acquired by J. Howard Marshall II in Great Northern Oil and Gas, which was the predecessor company to Koch Industries.[2]

In 1982, as an estate planning mechanism to reduce (or avoid) the cost of probate, J. Howard Marshall II placed almost all of his assets (including his interest in Marshall Associates, the family partnership that then held the Koch stock) in a revocable inter vivos trust, known as the J. Howard

[2] Koch Industries (Koch) is a privately held, integrated petroleum and chemical conglomerate headquartered in Wichita, Kansas. *See Marshall v. Marshall (In re Marshall)*, 275 B.R. 5, 13-16 (C.D. Cal. 2002) (describing in greater detail the creation and ownership of Koch Industries). In 1995, J. Howard Marshall II represented to Texas Commerce Bank that, through entities he controlled, he owned 14.7 percent of Koch. *Id.* at 15.

Marshall II Living Trust, or the Living Trust.[3] From 1982 until his death, J. Howard Marshall II executed a series of amended and restated instruments governing the terms of the Living Trust.

During his lifetime, J. Howard Marshall II retained the income from the Living Trust's assets, and the Living Trust was responsible for his debts. The terms of the Living Trust permitted J. Howard Marshall II to borrow money using the Living Trust's assets as security. Although the distributions from the Living Trust were his primary source of income, J. Howard Marshall II also drew a salary from Marshall Petroleum, Inc. (MPI), earned directors' fees from the corporate boards of which he was a member, and received minor pension payments.

The Living Trust also named the beneficiaries who would receive the Living Trust property after J. Howard Marshall II's death. At the time J. Howard Marshall II died, the primary beneficiary of the Living Trust was Pierce Marshall.[4]

[3] For some time, the shares of Koch stock were held by Marshall Associates. In 1984, the Koch stock and other assets owned by Marshall Associates were transferred to Marshall Petroleum, Inc. (MPI), a corporate entity created by J. Howard Marshall II and his first and second wives. The Living Trust also held J. Howard Marshall II's shares of MPI stock after its creation.

[4] Minor distributions from the Living Trust would also be made to various charities and family beneficiaries upon J. Howard Marshall II's death.

Also as part of his estate planning measures, J. Howard Marshall II executed a will that provided for the disposition of the assets that he held directly, i.e., not in the Living Trust or any other form of trust. J. Howard Marshall II executed his last will and testament relevant to these proceedings on December 22, 1992. This will contained pour-over provisions, which required the distribution of J. Howard Marshall II's probate estate to the Living Trust. Thus, the Living Trust was J. Howard Marshall II's primary estate planning document. Also in 1992, J. Howard Marshall II signed a document requesting that Pierce Marshall be appointed his guardian if a guardianship was ever warranted.

At the time J. Howard Marshall II met Vickie Lynn Marshall, essentially all of his assets were held by the Living Trust. J. Howard Marshall II modified his Living Trust for the last time on July 13, 1994, just a few days after his marriage. On that date, J. Howard Marshall II made the Living Trust irrevocable.[5]

[5] J. Howard Marshall II did, however, retain the limited power to make certain changes such as adding a charity as a beneficiary or substituting one beneficiary for another, as long as the beneficiary that was being substituted was already a beneficiary as of July 13, 1994. Thus, J. Howard Marshall II could have eliminated Pierce Marshall as a beneficiary of the Living Trust by substituting a charity in his place. J. Howard Marshall II could not, however, have added either his new wife or elder son as beneficiaries because they were not already beneficiaries as of July 13, 1994.

B

J. Howard Marshall II met Vickie Lynn (Smith) Marshall in October 1991. At the time, Vickie Lynn was a twenty-four year old divorcee and single mother living in Houston, Texas. She worked as a waitress and dancer to provide for her son, but she aspired to become an international superstar like her idol Marilyn Monroe. After a courtship lasting more than two years, J. Howard Marshall II and Vickie Lynn Marshall married on June 27, 1994.

Their union was short lived: J. Howard Marshall II died on August 4, 1995, of heart failure at the age of ninety. Although he lavished gifts and significant sums of money on Vickie Lynn Marshall during their courtship and marriage,[6] J. Howard Marshall II did not devise any real or personal property to her in his will, nor was a provision for distribution of income or principal of the Living Trust ever made in her favor. Similarly, J. Howard Marshall II did not give Vickie Lynn Marshall any interest in his business assets or stock holdings.

[6] On September 29, 1994, J. Howard Marshall II transferred gifts to Vickie Lynn Marshall out of his love and affection for her as his new wife. These gifts were valued at more than $6 million and included a ranch, several houses, cars, jewelry, and a substantial amount of cash. The gifts were memorialized in a document called the "Act of Donation." Vickie Lynn Marshall accepted these gifts on October 27, 1994.

J. Howard Marshall II also took steps to promote Vickie Lynn Marshall's career as a model.

C

In April 1995, before J. Howard Marshall II had died, Vickie Lynn Marshall filed suit against Pierce Marshall and others in Texas probate court, which was handling guardianship proceedings relating to J. Howard Marshall II. She alleged that Pierce Marshall was tortiously interfering with her statutory right to support from her husband and that Pierce Marshall had breached his fiduciary duties as a trustee of the Living Trust. She also asserted that Pierce Marshall used fraud and undue influence to have J. Howard Marshall II make the Living Trust irrevocable and make other estate planning changes that favored Pierce Marshall. By way of relief, Vickie Lynn Marshall sought the level of support to which she had become accustomed, a declaration from the court that J. Howard Marshall II was a beneficiary of the Living Trust, and the removal of Pierce Marshall from certain fiduciary capacities with respect to his father and his father's assets.

In August 1995, three days after J. Howard Marshall II died, Vickie Lynn Marshall added an application in the Texas probate court requesting that the court find that J. Howard Marshall II died intestate. Pierce Marshall opposed this application and petitioned for a declaration that his father's Living Trust and will were valid. Pierce Marshall offered J. Howard Marshall II's will for probate on August 16, 1995.

J. Howard Marshall III, J. Howard Marshall II's elder son, filed a will contest on December 20, 1995.[7] On January 23, 1998, Vickie Lynn Marshall joined this will contest. Several other individuals and institutional claimants brought actions seeking a share of J. Howard Marshall II's estate, but none are parties to this appeal.

By a third amended petition dated January 4, 2000, Vickie Lynn Marshall alleged that Pierce Marshall in his representative capacities, his attorneys, and others tortiously interfered with her expectation based upon her belief that J. Howard Marshall II had made oral promises to give her gifts both during his lifetime and upon his death.[8] In her third amended petition, Vickie Lynn Marshall again

[7] In 1980, J. Howard Marshall II and J. Howard Marshall III disagreed about the management of Koch Industries, and J. Howard Marshall III threatened to vote his father off the Board of Directors. To prevent this, J. Howard Marshall II bought the Koch stock back from J. Howard Marshall III for $8 million, an amount J. Howard Marshall II considered to be an exorbitant premium for stock he had gifted to his son years earlier. Following this dispute, J. Howard Marshall II changed his estate plan to exclude his elder son as a beneficiary under his will and Living Trust.

[8] Some of Vickie Lynn Marshall's claims in her third amended petition were made against Pierce Marshall in his individual capacity; because of the bankruptcy proceeding in California, however, Vickie Lynn Marshall limited her tortious interference claim in the Texas probate court to Pierce Marshall in his representative capacities.

challenged the validity of both the Living Trust, as amended, and J. Howard Marshall II's will.

D

After the Texas proceedings had commenced, but before she had filed her amended petition and will contest in that forum, Vickie Lynn Marshall filed for protection under federal bankruptcy laws in California, the state of which she claimed to be a resident. Vickie Lynn Marshall filed a voluntary chapter 11 bankruptcy petition in the United States District Court for the Central District of California on January 25, 1996. At this point, all non-exempt assets owned by Vickie Lynn Marshall, including her claims against J. Howard Marshall II's estate and against Pierce Marshall, constituted the bankruptcy estate.[9] *See* 11 U.S.C. § 541.

On May 7, 1996, Pierce Marshall commenced an adversary proceeding in the bankruptcy court seeking a declaration that in the event Vickie Lynn Marshall were to be found liable to Pierce Marshall for earlier instances of alleged defamation, her liability to him would not be dischargeable in her bankruptcy

[9] Although certain interested parties sought to have a trustee appointed to oversee Vickie Lynn Marshall's bankruptcy estate, the bankruptcy court denied the request. Instead, the bankruptcy court appointed an examiner to investigate all of Vickie Lynn Marshall's transactions and financial affairs and allowed Vickie Lynn Marshall to remain a "debtor in possession," holding her assets for the benefit of the bankruptcy estate.

proceeding.[10] *See* 11 U.S.C. § 523(a)(6). Specifically, Pierce Marshall filed a "complaint to determine dischargeability of debt pursuant to 11 U.S.C. § 523(a)(6)," in which he alleged that after J. Howard Marshall II's death Vickie Lynn Marshall and her attorneys "instituted a plan to obtain a quick recovery from the estate of J. Howard Marshall II by embarking on a tortious smear campaign against E. Pierce Marshall and his family." According to the complaint, Vickie Lynn Marshall's attorney expressed concern to a member of the press about the "blizzard of documents" that Pierce Marshall presented to his father in the days following his marriage to Vickie Lynn Marshall, noting that J. Howard Marshall II "signed [the documents] in an almost completely illegible fashion, which makes sense because he couldn't read at the time" and that "[t]he effect of it was basically an attempt to remove [J. Howard Marshall II] from control of his estate." The attorney further told a member of the press that "the law clearly entitles [Vickie Lynn Marshall] to half of whatever her late husband earned during the marriage" and described Pierce Marshall as "greedy and miserly" and a "real control freak." The complaint further alleges that the attorney knew the documents had been validly executed and effected J. Howard

[10] Pierce Marshall had filed suit against Vickie Lynn Marshall and her two attorneys in Texas court, but he dismissed Vickie Lynn Marshall from the suit without prejudice after she filed for bankruptcy.

Marshall II's estate planning wishes, but nevertheless suggested in the media that Pierce Marshall had engaged in one or more criminal acts in an effort to obtain his father's property. It also alleges that Vickie Lynn Marshall knew of the smear campaign efforts and in fact "participated in the civil conspiracy in an effort to extort a speedy settlement." By way of relief, Pierce Marshall specifically sought the following:

> 1. A determination that [Pierce Marshall's] claims against [Vickie Lynn Marshall] have not been discharged; 2. An order granting [Pierce Marshall] recovery for his reasonable costs and attorney's fees incurred herein and pre-and post-judgment interest as allowed by law; and 3. An order granting [Pierce Marshall] such other relief as is just.

On June 12, 1996, Pierce Marshall filed a proof of claim against Vickie Lynn Marshall's bankruptcy estate seeking an unliquidated amount of damages for his unsecured nonpriority claim arising from the alleged defamation. Attached to his proof of claim as "exhibit A" was his previously filed "complaint to determine dischargeability of debt pursuant to 11 U.S.C. § 523(a)(6)."[11] Two days later, on June 14,

[11] Pierce Marshall argues to us that he did not actually make a claim against Vickie Lynn Marshall's estate and, instead, sought only a determination of dischargeability. Like the district court, we, too, reject this argument. *See Marshall v. Marshall (In re Marshall),* 264 B.R. 609, 629 (C.D.Cal.2001). Pierce Marshall plainly filed a nondischargeability complaint,

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1996, Vickie Lynn Marshall's bankruptcy estate filed an answer to Pierce Marshall's nondischargeability complaint asserting a number of affirmative defenses, an objection to Pierce Marshall's creditor's claim, and counterclaims against Pierce Marshall in his individual capacity. Vickie Lynn Marshall asserted as an affirmative defense that "the statements complained of in this action are in fact substantially true, in whole and in part, and therefore cannot form the basis of a [defamation claim]."[12] Vickie Lynn Marshall's counterclaims included: tortious interference with her expectation of a gift or inheritance from J. Howard Marshall II; tortious interference with her rights as J. Howard Marshall II's spouse;

and then, more than a month later, he made a separate claim against the bankruptcy estate by filing his proof of claim for an unspecified amount of damages. Had he simply desired a nondischargeability determination, there would have been no reason to file a proof of claim seeking damages on the underlying defamation claim.

[12] She also asserted as an affirmative defense that:

> [The statements] were made in good faith, honestly, and not maliciously in that the signatures of J. Howard Marshall, II on the several documents allegedly signed by him shortly after his marriage to Mrs. Marshall were almost completely illegible; the physician of J. Howard Marshall, II has declared that [J. Howard Marshall II] could not read the typeface of the size used in the several documents at issue; the several documents allegedly signed by J. Howard Marshall, II did purport to give [Pierce Marshall] full control over the . . . Living Trust; and the several documents did purport to have the effect of transferring control over Mr. Marshall's estate.

breach of fiduciary duty; fraudulent transfer of J. Howard Marshall II's assets; abuse of the legal process; imprisoning J. Howard Marshall II against his will; breach of agreement and contract; and fraud, duress, and undue influence over J. Howard Marshall II.

Pierce Marshall moved to dismiss the counterclaims based on jurisdiction and also moved for the bankruptcy court to abstain from hearing the tortious interference claim. The bankruptcy court denied both motions.

Vickie Lynn Marshall entered into a settlement with her creditors, and the bankruptcy court confirmed Vickie Lynn Marshall's chapter 11 plan of reorganization on March 8, 1999.[13] The reorganization plan specifically provided that any proceeds from "disputed claims/interests" determined in Vickie Lynn Marshall's favor would be held by a disbursing agent to first satisfy creditors' claims, with any remaining amounts then going to Vickie Lynn Marshall. The reorganization plan also discussed the specific disbursement process for the "Marshall Claims," defined as those in the adversary proceeding initiated by Pierce Marshall.[14] In the order confirming the plan,

[13] This order was the subject of a separate appeal in this court. *Marshall v. Marshall (In re Marshall),* 119 F. App'x 136 (9th Cir. 2004).

[14] A complaint to determine the discharge of a debt coupled with an objection to a creditor's claim is an adversary proceeding. *See* Fed. R. Bankr. P. 3007, 7001.

the bankruptcy court discharged Vickie Lynn Marshall's preexisting debts and caused the property remaining in the bankruptcy estate to be revested in her.

Trial of the adversary proceeding began on October 27, 1999. *Marshall v. Marshall (In re Marshall),* 253 B.R. 550, 553 (Bankr. C.D. Cal. 2000). On November 5, 1999, the bankruptcy court granted summary judgment for Vickie Lynn Marshall on Pierce Marshall's adversary complaint, concluding that she did not publish or ratify any defamatory statements about him. *Marshall v. Marshall (In re Marshall),* 275 B.R. 5, 9 (C.D. Cal. 2002).

On September 27, 2000, the bankruptcy court found that Pierce Marshall had tortiously interfered with Vickie Lynn Marshall's expectation that she would inherit from J. Howard Marshall II's estate.[15] The bankruptcy court reasoned that a "widow's election" under Texas law supported a monetary judgment.[16] The court awarded Vickie Lynn Marshall

[15] The bankruptcy court entered a ruling only on Vickie Lynn Marshall's claim for tortious interference with her expectation of a gift. It does not appear that the bankruptcy court ever entered a ruling addressing Vickie Lynn Marshall's other various claims. Vickie Lynn Marshall did not appeal the bankruptcy court's judgment; thus, the claims that she abandoned would now seem to be barred.

[16] Vickie Lynn Marshall's community property interest in J. Howard Marshall II's income from his separate property was approximately $1 million. Because J. Howard Marshall II gifted

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$449,754,134, but stated that the final calculation of damages remained to be determined after completion of the Texas probate action.

On October 6, 2000, the bankruptcy court entered a revised judgment against Pierce Marshall in his individual capacity, again for $449,754,134, less whatever proceeds Vickie Lynn Marshall received from J. Howard Marshall II's estate. In its revised judgment the bankruptcy court did not rely on Vickie Lynn Marshall's "widow's election," but concluded based upon "a preponderance of the evidence admitted at trial and the findings imposed as sanctions against Pierce Marshall for discovery abuses, that Pierce . . . tortiously deprived [Vickie Lynn Marshall] of her expectancy of a substantial *inter vivos* gift from her deceased husband."[17] On December 29, 2000, the

her property during their marriage in excess of this amount, Vickie Lynn Marshall did not file a community property claim.

[17] The bankruptcy court imposed various sanctions on Pierce Marshall for perceived discovery abuses. These sanctions included, in addition to factual findings made against him, limiting Pierce Marshall's ability to introduce percipient witnesses and present certain evidence on the merits of the claims levied against him. Our discussion of these matters will be limited because the parties agreed that there are no sanctions issues before us on appeal.

We further note that, when it took additional evidence on the case, the district court likewise limited to some extent the testimony and evidence Pierce Marshall was able to introduce. Pierce Marshall claims that the district court violated his due process rights with this ruling and other evidentiary decisions. Because we conclude that Pierce Marshall is entitled to

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bankruptcy court entered a judgment against Pierce Marshall in the amount of $474,754,134. A timely appeal of this ruling to the federal district court followed.

E

Proceedings in the Texas probate court continued unabated during Vickie Lynn Marshall's bankruptcy in California. On January 5, 2001, days after the bankruptcy court entered its judgment, Vickie Lynn Marshall filed a voluntary nonsuit of all her claims against Pierce Marshall in the Texas probate proceeding. The probate judge explained to Vickie Lynn Marshall's counsel that, by doing so, she would be giving up any claim to money that was in her late husband's estate and any claim that the Living Trust or will were invalid. The Texas probate judge warned her in open court as follows:

> Even if you take a nonsuit, which under the Rules of Civil Procedure give you a right to refile it, as a practical matter you don't, because the Estate is gone. . . . Your claim to anything that [J. Howard Marshall II] had at any time in his life is over when this final judgment is signed. The fact that the Rules of Civil Procedure allow you to take a nonsuit and re-file later doesn't really apply

judgment in his favor for other reasons, we need not address his due process claim.

> in Probate Court when we're talking about who is entitled to an Estate.

Despite the probate court's warnings, and in apparent reliance on her belief that the bankruptcy court had the authority to enter a final judgment on the counterclaim against Pierce Marshall, Vickie Lynn Marshall elected to dismiss her claims against J. Howard Marshall II's estate and against Pierce Marshall both individually and in his representative capacities.[18]

On February 9, 2001, with the leave of the Texas probate court, Pierce Marshall filed an amended counterclaim against Vickie Lynn Marshall for declaratory relief to determine her rights as to the estate and property of J. Howard Marshall II. Pierce Marshall also sought a declaratory judgment against Vickie Lynn Marshall and J. Howard Marshall III that J. Howard Marshall II's Living Trust and will reflected his true intentions and were valid. Thus, Vickie Lynn Marshall remained in the probate proceedings as a defendant to Pierce Marshall's counterclaims. The Texas probate court held a five-month jury trial in which all parties, including Vickie Lynn Marshall, fully participated.[19] On March 7,

[18] Vickie Lynn Marshall also moved to dismiss other counterclaims against her in the Texas probate court, but the probate court denied her motion.

[19] Vickie Lynn Marshall vigorously argued against the validity of the Living Trust in the Texas probate court. For example, prior to trial, Vickie Lynn Marshall submitted her

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2001, the Texas jury returned its verdict. The jury unanimously answered a number of special verdict questions, making the following factual findings: (1) the Living Trust and will were valid and had not been forged or altered; (2) J. Howard Marshall II had not been the victim of fraud or undue influence; (3) he had the requisite mental capacity when he executed his Living Trust and will; and (4) he did not have an agreement with Vickie Lynn Marshall that he would give her one-half of all his property.

The Texas probate court entered a final judgment in accordance with the jury's verdict on August 15, 2001. Subsequently, the probate court amended its judgment on two occasions, the last being entered on December 7, 2001. In the second amended judgement, the Texas probate court found that the will and Living Trust, as amended, were valid and not the product of undue influence. The probate court concluded as a matter of law:

preliminary proposed jury interrogatories, which included instructions and jury queries on tortious interference with a gift expectancy and on fraud, duress, and undue influence. In his opening statement, Vickie Lynn Marshall's counsel explained to the jury that this was a case "about tortious interference with an intent to give an *inter vivos* gift." He told the jury Vickie Lynn Marshall would testify that J. Howard Marshall II promised her "half of everything that he had." Vickie Lynn Marshall presented her case in chief in great detail over approximately 60 hours. After she nonsuited her affirmative claims, she continued to defend against Pierce Marshall's counterclaims.

> that Vickie Lynn Marshall does not possess any interest in and is not entitled to possession of any property within the estate of J. Howard Marshall II or [the Living Trust] because of any representations, promises or agreements made by J. Howard Marshall II; . . .
>
> that any and all claims that have been or should have been asserted by Vickie Lynn Marshall . . . based upon alleged representations, promises, or agreements made by J. Howard Marshall II to or with Vickie Lynn Marshall . . . have been disposed of in this proceeding; . . .
>
> that J. Howard Marshall did not intend to give and did not give to Vickie Lynn Marshall . . . a gift or bequest from the Estate of J. Howard Marshall II or from the [Living Trust] either prior to or upon his death; . . .
>
> that Vickie Lynn Marshall . . . shall take nothing from any claim that she should have made in this proceeding as a compulsory counterclaim against . . . E. Pierce Marshall.

Accordingly, the Texas probate court entered judgment in favor of Pierce Marshall on all claims and held that Pierce Marshall was entitled to his inheritance, free from all claims by Vickie Lynn Marshall or J. Howard Marshall III.

F

Pierce Marshall appealed the bankruptcy court's judgment to the district court, which asserted original bankruptcy jurisdiction. 28 U.S.C. § 1334. After the Texas probate court entered its final judgment, Pierce Marshall moved to dismiss Vickie Lynn Marshall's claims against him in the district court based on principles of claim and issue preclusion.

On June 19, 2001, the district court issued an opinion and order affirming the bankruptcy court's determination that it had federal jurisdiction over Vickie Lynn Marshall's claim of tortious interference with the expectation of a gift. *Marshall v. Marshall (In re Marshall),* 264 B.R. 609, 619-21 (C.D. Cal. 2001). The district court also held that the Texas probate court had not ruled on Vickie Lynn Marshall's claim against Pierce Marshall in his individual capacity. *See id.* at 621-24, 633 & n.24. The district court went on to reverse the bankruptcy court's determination that the bankruptcy court could enter a final judgment on the claim as a "core" bankruptcy proceeding. *Id.* at 632-33. The district court recognized that Vickie Lynn Marshall's claim arguably arose out of the same factual transaction as that of Pierce Marshall, but it reasoned that the "connection [was] attenuated" and "the reasons for why counterclaims arising out of the same transaction should usually be considered core do not apply." *Id.* at 631-32. The court explained that the attenuated factual nexus between the claims, the different legal theories underlying the claims, the fact

that Vickie Lynn Marshall's claim dwarfed Pierce Marshall's claim in terms of recovery sought and evidence required to establish it, and Ninth Circuit jurisprudence cautioning courts to avoid characterizing a proceeding as core if to do so would raise constitutional problems, all counseled in favor of classifying Vickie Lynn Marshall's counterclaim as non-core. *Id.* at 625-32. Because bankruptcy courts may only issue proposed findings of fact and conclusions of law in non-core matters (absent the parties' consent), the district court vacated the bankruptcy court's entry of judgment. *Id.* at 632-33.

On December 21, 2001, the district court denied Pierce Marshall's motion for summary judgment based on claim and issue preclusion. *Marshall v. Marshall (In re Marshall),* 271 B.R. 858 (C.D. Cal. 2001).

After receiving additional evidence on Vickie Lynn Marshall's claim, the district court entered judgment in her favor on March 7, 2002. The district court found that "J. Howard always intended to give Vickie . . . half of his 'new community,'" a term he created to mean the growth of his assets during the time of their marriage. *In re Marshall,* 275 B.R. at 29 & n.19, 52. The district court found that the circumstantial evidence before it "sufficiently establishes the existence of a draft 'catchall trust' instrument" prepared by J. Howard Marshall II's attorney as a means of effecting this gift of new community. *Id.* at 26-29, 26 n.17. The district court further found that Pierce Marshall, in concert with an

attorney, "backdated documents, altered documents, destroyed documents, suborned falsified notary statements, presented documents to [J. Howard Marshall II] under false pretenses, and committed perjury," all in an effort to prevent his father from giving this gift of new community to Vickie Lynn Marshall. *Id.* at 53. The district court found that J. Howard Marshall II was "duped" by this fraudulent conduct into making various estate planning changes, such as making the Living Trust irrevocable. *See id.* at 42-50. Based on this and other factual findings, the district court determined that Pierce Marshall had tortiously interfered with Vickie Lynn Marshall's expectancy of an inter vivos gift from J. Howard Marshall II. *Id.* at 58.

The district court awarded Vickie Lynn Marshall damages based upon what it believed she would have received as a gift from J. Howard Marshall II, absent the purported interference. The award consisted of $44,292,767.33 in compensatory damages and an equal amount in punitive damages, for a total of $88,585,534.66, plus costs of suit. *In re Marshall,* 275 B.R. at 58.

G

Pierce Marshall appealed the district court's judgment, and Vickie Lynn Marshall cross-appealed. Believing that the probate exception to federal subject matter jurisdiction precluded our consideration of the case, we vacated the judgment and

remanded with instructions that the district court order the bankruptcy court to vacate its judgment against Pierce Marshall. *Marshall v. Marshall (In re Marshall),* 392 F.3d 1118, 1137-38 (9th Cir. 2004).

The United States Supreme Court granted certiorari "to resolve the apparent confusion among federal courts concerning the scope of the probate exception." *Marshall v. Marshall,* 547 U.S. 293, 305 (2006). The Supreme Court concluded that the probate exception did not apply, reversed our decision, and remanded for us to consider the merits of the case, including the question "whether Vickie's claim was 'core' " and "Pierce's arguments concerning claim and issue preclusion." *Id.* at 314-15; *see also id.* at 313 n.5 (discussing Texas appellate cases that found tortious interference claims to be "barred" after "applying ordinary principles of preclusion" and stating that, in this case, the "matter of preclusion remains open on remand").

We ordered supplemental briefing on these and other issues and held oral argument on June 25, 2009.[20]

[20] In addition to the supplemental briefs filed by the parties, we also received two thoughtful amicus briefs filed in support of Pierce Marshall. The first brief, filed by Professors of Law S. Todd Brown, G. Marcus Cole, Ronald D. Rotunda, and Todd J. Zywicki, discusses "the proper distinction between 'core' and 'non-core' bankruptcy proceedings – and the application of that distinction to counterclaims like the one in this case." Professors' Amicus Br. at 2. The second brief, filed by the Washington Legal

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II

"We review de novo questions of law." *Forest Grove Sch. Dist. v. T.A.*, 523 F.3d 1078, 1083 (9th Cir. 2008); *see In re Valdez Fisheries Dev. Ass'n, Inc.*, 439 F.3d 545, 547 (9th Cir. 2006) (bankruptcy court's determination of its jurisdiction); *Kendall v. Visa U.S.A., Inc.*, 518 F.3d 1042, 1050 (9th Cir. 2008) (issue preclusion); *Siegel v. Fed. Home Loan Mortgage Corp.*, 143 F.3d 525, 528 (9th Cir. 1998) (claim preclusion). We review a district court's findings of fact for clear error, reversing only if "left with the definite and firm conviction that a mistake has been committed." *Easley v. Cromartie*, 532 U.S. 234, 242 (2001).

III

Pierce Marshall argues that the district court correctly concluded that Vickie Lynn Marshall's tortious interference counterclaim was a non-core proceeding for which the bankruptcy court could issue only proposed findings of fact and conclusions of law. Pierce Marshall further argues that the district court erred, however, when it refused to give any preclusive effect to the Texas probate court's judgment, which was issued while the case was pending before the district court. Vickie Lynn Marshall responds by

Foundation, explained its concern "that the district court's refusal to give preclusive effect to the Texas judgment undermines the principles of federalism and contravenes the Full Faith and Credit Act." Wash. Legal Found. Amicus Br. at 1.

arguing that her counterclaim is a core proceeding, that the bankruptcy court properly entered a final judgment on it well before the Texas probate court's judgment, and that preclusion principles therefore do not apply.

A

For parties whose views seldom correspond, both sides appear to share the position that the determination whether Vickie Lynn Marshall's counterclaim is "core" or "non-core" is central to the disposition of this case and will affect the manner in which our analysis proceeds. We agree. For the reasons detailed below, we conclude that Vickie Lynn Marshall's counterclaim is a non-core proceeding that is, at most, related to her bankruptcy case.

1

In an article discussing the Bankruptcy Code, Professor Vern Countryman wrote, "To understand how we got where we are, it is necessary to understand where we were." Vern Countryman, *Scrambling to Define Bankruptcy Jurisdiction,* 22 Harv. J. on Legis. 1, 2 (1985). This statement holds true today: one must have some familiarity with the evolution of the current bankruptcy regime in order to appreciate the important distinctions between "arising under," "arising in," and "related to" proceedings and how the notion of "core" proceedings came to exist.

The Bankruptcy Act of 1898 is the basis for modern bankruptcy law. 30 Stat. 544 (repealed 1979); *see* Collier on Bankruptcy ¶ 1.0[1] (15th Ed. Revised 2007). It designated the district courts as the "courts of bankruptcy" and created the office of the referee to assist the district courts in the discharge of their duties. Bankruptcy Act of 1898 §§ 1-2, 33-43. The Act gave the referees jurisdiction, "subject always to a review by the judge," *id.* § 38, "to perform all duties conferred on 'courts of bankruptcy' as distinguished from those conferred on 'judges,' which were to be performed only by district judges." Countryman, *supra,* at 2-3; *see* Bankruptcy Act of 1898 §§ 1(20), 38.

The jurisdiction exercised by "courts of bankruptcy" (and, in turn, bankruptcy referees) under the 1898 scheme was customarily referred to as "summary jurisdiction." Countryman, *supra,* at 2-4. This "summary jurisdiction" covered three general areas: (1) handling administrative proceedings in the bankruptcy case, such as accepting the bankruptcy petition, allowing claims, granting discharges, and confirming debt adjustment plans, etc., Bankruptcy Act of 1898 §§ 2, 38; *see, e.g., U.S. Fidelity & Guaranty Co. v. Bray,* 225 U.S. 205, 218 (1912), (2) resolving controversies over property in the actual or constructive possession of the court, Bankruptcy Act of 1898 §§ 2, 38; *see, e.g., Thompson v. Magnolia Petroleum Co.,* 309 U.S. 478, 481 (1940), and (3) deciding, "by consent of the defendant," actions brought by the bankruptcy trustee that were "plenary in character" because the bankrupt could have

brought them in another forum in the absence of the bankruptcy proceedings, Bankruptcy Act of 1898 § 23b; *MacDonald v. Plymouth County Trust Co.*, 286 U.S. 263, 266-67 (1932); *see also* Countryman, *supra*, at 2-3.[21]

Bankruptcy proceedings under the 1898 Act "were generally conducted before referees, except in those instances in which the district court elected to withdraw a case from a referee." *N. Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 53 (1982). The district court presided over any appeal from a referee's final order. *Id.*

In 1978, Congress passed the Bankruptcy Reform Act, which eliminated the referee system and established "in each judicial district, as an adjunct to the district court for such district, a bankruptcy court which shall be a court of record known as the United States Bankruptcy Court for the district." *Id.* (quoting 28 U.S.C. § 151(a) (Supp. IV 1981)). The 1978 Act eliminated the distinction between "summary" bankruptcy jurisdiction and "plenary" jurisdiction, and it "grant[ed] the new courts jurisdiction over all 'civil proceedings arising under title 11 [the Bankruptcy title] or arising in or related to cases under title 11.'" *Id.* at 54 (second alteration in

[21] An example of a "plenary matter" that could be heard by consent of the parties was a "dispute[ ] involving property in the possession of a third person." *N. Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 53 (1982).

original) (emphasis omitted) (quoting 28 U.S.C. § 1471(b) (Supp. IV 1981)); *see also* 28 U.S.C. § 1471(b) (Supp. IV 1981) (noting that the district courts' jurisdiction was "original but not exclusive"). With limited exception, under the 1978 Act, the judges of the bankruptcy courts had "all of the 'powers of equity, law, and admiralty.'" *Id.* at 55 (quoting 28 U.S.C. § 1481 (Supp. IV 1981)).

The most important provision of the 1978 Act was § 1471(c), which provided that "[t]he bankruptcy court . . . shall exercise all of the jurisdiction conferred by this section on the district courts." 28 U.S.C. § 1471 (Supp. IV 1981). Congress knew that this provision raised serious constitutional concerns because it permitted an Article I tribunal to exercise the same jurisdiction bestowed upon an Article III court, but the risk of invalidation was deemed worth achieving the goal of setting up a faster and cheaper method to accomplish reorganization. *See* Countryman, *supra,* at 7-9; *see also* H.R. Rep. No. 95-595, at 5968 (1977) (acknowledging "serious constitutional doubts" raised by the full grant of jurisdiction under the proposed bankruptcy system to non-Article III judges).

The risk of invalidation was soon realized. In *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.,* the Supreme Court considered whether the Constitution permitted the bankruptcy court to exercise jurisdiction over a state law breach of contract claim filed by the debtor in possession against a third party who was a stranger to the

bankruptcy proceeding. 458 U.S. 50 (1982). The plurality explained that the Bankruptcy Act of 1978 impermissibly shifted essential attributes of judicial power from the Article III district court to the non-Article III bankruptcy court. *Id.* at 87. The holding of six justices in *Marathon* is fairly well summarized in a footnote to the plurality opinion:

> [A]t the least, the new bankruptcy judges cannot constitutionally be vested with jurisdiction to decide this state-law contract claim against Marathon. As part of a comprehensive restructuring of the bankruptcy laws, Congress has vested jurisdiction over this and all matters related to cases under Title 11 in a single non-Art. III court, and has done so pursuant to a single statutory grant of jurisdiction. In these circumstances we cannot conclude that if Congress were aware that the grant of jurisdiction could not constitutionally encompass this and similar claims, it would simply remove the jurisdiction of the bankruptcy court over these matters, leaving the jurisdictional provision and adjudicatory structure intact with respect to other types of claims, and thus subject to Art. III constitutional challenge on a claim-by-claim basis. Indeed, we note that one of the express purposes of the Act was to ensure adjudication of all claims in a single forum and to avoid the delay and expense of jurisdictional disputes. Nor can we assume, as THE CHIEF JUSTICE suggests that Congress' choice would be to have these cases "routed to the

> United States district court of which the bankruptcy court is an adjunct." We think that it is for Congress to determine the proper manner of restructuring the Bankruptcy Act of 1978 to conform to the requirements of Art. III in the way that will best effectuate the legislative purpose.

458 U.S. at 88 n.40 (Brennan, J., plurality) (joined by Justices Marshall, Blackmun, and Stevens) (citations omitted); *see also id.* at 91-92 (Rehnquist, J., concurring) (joined by Justice O'Connor). The Court stayed its judgment in *Marathon* for six months to allow Congress the opportunity to remedy the constitutional flaws in the 1978 Act's grant of jurisdiction to the bankruptcy courts. *Id.* at 88.

Congress did not act in time, and the Court's mandate took effect. Faced with the potential collapse of the bankruptcy system, the Judicial Conference "adopt[ed] a resolution requiring the Director of the Administrative Office of the United States Courts to 'provide each circuit with a proposed rule' which was to take effect [as a local rule] in the absence of congressional action." Countryman, *supra,* at 19; *see* Collier ¶ 3.01[2][b][ii] & n.16 (discussing the emergency rule and reproducing its text). The purpose of this resolution was "to permit the bankruptcy system to continue without disruption in reliance on jurisdictional grants remaining in the law as limited by" *Marathon. Countryman, supra,* at 19.

The Emergency Rule continued the bankruptcy system established by the 1978 Act with the exception

of how "related proceedings" like the contract claim in *Marathon* would be treated. *See* Collier ¶ 3.01[2][b][ii] & n.16. The Emergency Rule defined "related proceedings" as "those civil proceedings that, in the absence of a petition in bankruptcy, could have been brought in a district court or state court."[22] Emergency Rule § d(3)(A), *reproduced at* Collier ¶ 3.01[2][b][ii] n.16. The Emergency Rule prohibited bankruptcy judges from entering a judgment or dispositive order on related proceedings; instead, the bankruptcy court was to "submit findings, conclusions, and a proposed judgment or order to the district judge, unless the parties to the proceeding consent to entry of the judgment or order by the bankruptcy judge." Emergency Rule § d(3)(B), *reproduced at* Collier ¶ 3.01[2][b][ii] n.16.

More than two years after the *Marathon* decision, Congress finally passed the Bankruptcy Amendments

[22] The Emergency Rule went on to explain that:

> Related proceedings include, but are not limited to, claims brought by the estate against parties who have not filed claims against the estate. Related proceedings do not include: contested and uncontested matters concerning the administration of the estate; allowance of and objections to claims against the estate; counterclaims by the estate in whatever amount against persons filing claims against the estate. . . . A proceeding is not a related proceeding merely because the outcome will be affected by state law.

Emergency Rule § d(3)(A), *reproduced at* Collier ¶ 3.01[2][b][ii] n.16.

and Federal Judgeship Act of 1984. Pub. L. No. 98-353 (HR 5174), 98 Stat. 333 (1984). The 1984 Act, with amendments not relevant to this proceeding, governs the dispute before us.

[1] Under the 1984 Act the district court continues to have original jurisdiction over all cases under title 11 and "all civil proceedings arising under title 11, or arising in or related to cases under title 11." 28 U.S.C. § 1334(a)-(b). The district court, in turn, may refer "any or all cases under title 11 and any or all proceedings arising under title 11 or arising in or related to a case under title 11" to the bankruptcy court. *Id.* § 157(a). Thus, as under the 1978 Act, the bankruptcy court's subject matter jurisdiction under the 1984 Act is coterminous with that of the district court. *See id.* §§ 157(a), 1334; *Fietz v. Great W. Sav. (In re Fietz)*, 852 F.2d 455, 457 (9th Cir. 1988).

The manner in which the bankruptcy court may exercise its delegated jurisdiction under the 1984 Act, however, differs greatly from its 1978 predecessor. In an obvious effort to comply with the principles of *Marathon*, gone is the problematic provision from the 1978 Act empowering the bankruptcy court to exercise "all of the jurisdiction" of the district court. 28 U.S.C. § 1471 (Supp. IV 1981). Instead, subsections (b) and (c) to § 157 prescribe the manner in which the bankruptcy court may exercise its delegated jurisdiction by identifying those situations (1) when the bankruptcy court is authorized to issue a final order disposing of some or all of the matters

before it and (2) when the bankruptcy court is empowered only to make a report and recommendation to the district court. 28 U.S.C. § 157(b)-(c); *see also* Countryman, *supra,* at 35 (noting that like the Emergency Rule, the 1984 Act distinguishes between "when the bankruptcy judge can act as a judge" and "when he acts only as a special master").

[2] Section 157(b)(1) provides that "Bankruptcy judges may hear and determine all cases under title 11 and all *core proceedings arising under* title 11, or *arising in* a case under title 11" that are referred to it by the district court.[23] 28 U.S.C. § 157(b)(1) (emphasis

[23] The term "core" has its roots in Justice Brennan's plurality in *Marathon*. 458 U.S. at 71, 102 S.Ct. 2858 (referring to matters "at the core of federal bankruptcy power"). There, Justice Brennan concluded that the statutory grant of "causes of action owned by the debtor at the time of the petition for bankruptcy" could not be squared with the separation of powers doctrine, which requires that Article III federal judicial power be vested in Article III judges. *Id.* at 54, 62, 76, 84, 87. Justice Brennan went on to explore "three narrow" exceptions to the separation of powers doctrine that permitted the use of "legislative courts" because of the appellant's argument that the bankruptcy courts could have been so constituted. *Id.* at 63-64. One exception was for territorial courts in "certain geographical areas, in which no State operated as sovereign" such as the District of Columbia, Indian tribal courts, and consular courts. *Id.* at 64-65. The second exception was for the establishment of military courts-martial. *Id.* at 66. The third exception was for adjudications involving "public rights," which are those matters that "aris[e] between the Government and persons subject to its authority in connection with the performance of the constitutional functions of the executive or legislative departments, and . . . that historically could have been determined exclusively by

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added). In subsection (b)(2) Congress provided a non-exhaustive definition of core proceedings that includes the omnibus categories of "matters concerning the administration of the estate" and "other proceedings affecting the liquidation of assets of the estate." *Id.* § 157(b)(2)(A), (O);[24] *Harris v. Wittman*

those departments." *Id.* at 67-68 (internal citations and quotations omitted).

In contrast, Justice Brennan explained that "the liability of one individual to another under the law as defined, is a matter of private rights. . . . Private-rights disputes . . . lie at the core of the historically recognized judicial power." *Id.* at 69-70. He further cautioned that "the restructuring of debtor-creditor relations, *which is at the core of the federal bankruptcy power,* must be distinguished from the adjudication of state-created private rights, such as the right to recover contract damages that is at issue in this case. The former may well be a 'public right,' but the latter obviously is not." *Id.* at 71 (emphasis added).

The Supreme Court has not explicitly held that the restructuring of debtor-creditor relations is a public right. *See Granfinanciera v. Nordberg,* 492 U.S. 33, 56 n.11 (1989) ("We do not suggest that the restructuring of debtor-creditor relations is in fact a public right. This thesis has met with substantial scholarly criticism . . . and we do not seek to defend it here.").

[24] In full, subsection (b)(2) provides as follows:

> Core proceedings include, but are not limited to –
>
> (A) matters concerning the administration of the estate;
>
> (B) allowance or disallowance of claims against the estate or exemptions from property of the estate, and estimation of claims or interests for the purposes of confirming a plan under chapter 11,

(Continued on following page)

12, or 13 of title 11 but not the liquidation or estimation of contingent or unliquidated personal injury tort or wrongful death claims against the estate for purposes of distribution in a case under title 11;

(C) counterclaims by the estate against persons filing claims against the estate;

(D) orders in respect to obtaining credit;

(E) orders to turn over property of the estate;

(F) proceedings to determine, avoid, or recover preferences;

(G) motions to terminate, annul, or modify the automatic stay;

(H) proceedings to determine, avoid, or recover fraudulent conveyances;

(I) determinations as to the dischargeability of particular debts;

(J) objections to discharges;

(K) determinations of the validity, extent, or priority of liens;

(L) confirmations of plans;

(M) orders approving the use or lease of property, including the use of cash collateral;

(N) orders approving the sale of property other than property resulting from claims brought by the estate against persons who have not filed claims against the estate;

(O) other proceedings affecting the liquidation of the assets of the estate or the adjustment of the debtor-creditor or the equity security holder relationship, except personal injury tort or wrongful death claims; and

(P) recognition of foreign proceedings and other matters under chapter 15 of title 11.

28 U.S.C. § 157(b)(2).

(In re Harris), 590 F.3d 730, 738 (9th Cir. 2009). Congress also indicated that a matter may be a core proceeding even if its outcome may be affected by state law. *See* 28 U.S.C. § 157(b)(3).

[3] By way of comparison, § 157(c)(1) authorizes the bankruptcy judge to "hear a proceeding that is *not a core proceeding but that is otherwise related to* a case under title 11." *Compare id.* § 157(c)(1) (emphasis added), *with id.* § 157(b)(1) (authorizing the bankruptcy court to "hear *and determine* "certain matters) (emphasis added). For proceedings falling within § 157(c)(1), the bankruptcy court is empowered only to "submit proposed findings of fact and conclusions of law to the district court." *Id.* § 157(c)(1). Thus, unless the parties consent to final determination by the bankruptcy judge, *id.* § 157(c)(2), the responsibility to "determine" a "[non-]core proceeding that is otherwise related to a case under title 11" always remains with the district court, *id.* § 157(c)(1) ("[A]ny final order or judgment shall be entered by the district judge after considering the bankruptcy judge's proposed findings and conclusions and after reviewing de novo those matters to which any party has timely and specifically objected.").

[4] The 1984 Act does not specifically detail what it means for a civil proceeding to "arise under title 11," "arise in a case under title 11," "or relate [ ] to a case under title 11." Our case law, however, holds that proceedings "arise under title 11" if they "involve a cause of action created or determined by a statutory provision of title 11." *In re Harris*, 590 F.3d at 737. On

the other hand, civil proceedings "arise in a case under title 11" when they are "not based on any right expressly created by title 11, but nevertheless, would have no existence outside of the bankruptcy." *In re Eastport Assocs.*, 935 F.2d 1071, 1076-77 (9th Cir. 1991) (quoting *In re Wood*, 825 F.2d 90, 96-97 (5th Cir. 1987)); *see In re Harris*, 590 F.3d at 737.[25] Like the Fourth, Fifth, and Eight Circuit Courts of Appeal, we adopted without modification the Third Circuit's definition of what constitutes a "related" proceeding:

> The usual articulation of the test for determining whether a civil proceeding is related to bankruptcy is whether the outcome of the proceeding could conceivably have any effect on the estate being administered in bankruptcy. . . . An action is related to bankruptcy if the outcome could alter the debtor's right, liabilities, options, or freedom of action (either positively or negatively) and which in any way impacts upon the handling and administration of the bankrupt estate.

[25] *See In re Goodman*, 991 F.2d 613, 616-17 (9th Cir. 1993) (discussing *In re Eastport Associates* and proceedings arising under title 11 or arising in a case under title 11); *see also* H.R. Rep. No. 95-595, at 6401 (Sept. 8, 1977) ("The phrase 'arising under' has a well defined and broad meaning in the jurisdictional context. By a grant of jurisdiction over all proceedings arising under title 11, the bankruptcy courts will be able to hear any matter under which a claim is made under a provision of title 11."); Collier ¶ 3.01[4][c][i] (statutory language suggests that civil proceedings arise under title 11 "when the cause of action is one that is created by title 11").

In re Fietz, 852 F.2d 455, 457 (9th Cir. 1988) (quoting *Pacor, Inc. v. Higgins,* 743 F.2d 984, 994 (3d Cir. 1984)).

With this constitutional and statutory backdrop in mind, we turn to the question before us today: whether the bankruptcy judge could "hear and determine," as a "core proceeding[] arising under title 11, or arising in a case under title 11," Vickie Lynn Marshall's counterclaim for tortious interference against Pierce Marshall.

2

Pierce Marshall takes the position that even if a counterclaim is asserted in response to a proof of claim against the bankruptcy estate, such that it meets Congress' definition of a core proceeding contained in § 157(b)(2)(C), the bankruptcy court cannot exercise "final order" jurisdiction over it under § 157(b)(1) unless the counterclaim "arises under" or "arises in a case under" the Bankruptcy Code. Pierce Marshall argues that Vickie Lynn Marshall's claim neither "arises under" nor "arises in a case under" the Bankruptcy Code: it is a state law counterclaim that could have been brought and was brought, at least in part, in a non-bankruptcy forum. Because there is nothing unique to bankruptcy about her claim, Pierce Marshall argues that the bankruptcy court could not, consistent with the Constitution, the *Marathon* decision, and the bankruptcy court's statutory grant

of power in § 157(b)(1), enter a final judgment against him.

We agree with Pierce Marshall that our case law presents a two-step approach. A bankruptcy judge may only determine a claim that meets Congress' definition of a core proceeding *and* arises under or arises in title 11. *See In re Harris,* 590 F.3d at 737-41. We disagree, however, with Pierce Marshall's argument that the fact that Vickie Lynn Marshall's counterclaim could have been brought in state court and was not a bankruptcy-specific claim automatically renders the claim non-core. This approach goes too far and may render § 157(b)(2)(C) superfluous.[26] Under Pierce Marshall's narrow reading of the statute it is difficult to imagine a counterclaim against a person filing against the estate that "arises under" the Bankruptcy Code or "arises in a case under" the Bankruptcy Code and that is not already covered by a more specific provision of § 157(b)(2).

[26] This concern was appropriately shared by the district court, which wrote:

> Thus, on one hand, calling any counterclaim that falls within the literal language of the statute core seems to contradict the holding of *Marathon*. On the other hand, calling any counterclaim that could have been asserted as an independent lawsuit seems to render § 157(b)(2)(C) itself nugatory, because any counterclaim could have been asserted as a separate lawsuit absent the filing of the bankruptcy petition. *Collier* notes this problem and states that "[t]he matter is still unsettled."

In re Marshall, 264 B.R. at 630.

Many creditor claims filed against a bankruptcy estate are based upon state law, not the Bankruptcy Code or something else that is unique to the bankruptcy context.[27] We do not believe that Congress intended § 157(b)(2)(C) to be a meaningless (or near meaningless) provision, which is what it would become under Pierce Marshall's overly restrictive approach. *See United Sav. Ass'n v. Timbers of Inwood Forest Assocs., Ltd.*, 484 U.S. 365, 370-71 (1988) (construing several sections of the Bankruptcy Code and observing that "[s]tatutory construction . . . is a holistic endeavor"); *see also Dole Food Co. v. Patrickson,* 538 U.S. 468, 477 (2003) (cautioning against construing a "statute in a manner that is strained and, at the same time, would render a statutory term superfluous").

Harris may seem to provide some validity to Pierce Marshall's argument because that decision relied on the fact that the contract claim "arose from the administration of [the] bankruptcy estate." *In re Harris,* 590 F.3d at 740. However, in *Harris* we required a bankruptcy nexus only because there we dealt with § 157(b)(2)(A), one of the "catchall" provisions. *See id.* at 739-41. Section 157(b)(2)(A)

[27] Indeed, Congress' awareness of this fact is reflected in its expressed desire that a determination of whether something is a "core proceeding under this subsection [§ 157(b)] or is a proceeding that is otherwise related to a case under title 11 [§ 157(c)] . . . not be made solely on the basis that its resolution may be affected by State law." *See* 28 U.S.C. § 157(b)(3).

refers to "matters concerning the administration of the [bankruptcy] estate." *Harris* relied on earlier precedent to determine that if the only applicable provision in § 157(b)(2) is one of the catchall provisions, the claim must literally fit within the wording of the catchall provision to be considered core. *See Harris,* 590 F.3d at 740. Here, we do not deal with the catchall provisions of § 157(b)(2) but with one of the specific provisions, § 157(b)(2)(C). Thus, although Vickie Lynn Marshall's counterclaim for tortious interference could have been brought independently from the bankruptcy proceeding and was not unique to the bankruptcy context, we have not reached the end of our inquiry.

While Pierce Marshall's approach is too narrow, Vickie Lynn Marshall's is too expansive. She takes the position that her counterclaim falls within the plain language definition of a "core proceeding" as a "counterclaim[ ] by the estate against persons filing claims against the estate." 28 U.S.C. § 157(b)(2)(C). As far as Vickie Lynn Marshall is concerned, that should end the matter because the "'core proceedings' listed in § 157(b), by definition, meet the arising in/arising under standard." Vickie Lynn Marshall Supplemental Br. at 6. Her criticism of Pierce Marshall's two step approach finds some support in the fact that few courts consider separately the questions whether something is a "core proceeding" and whether it "arises under" the Bankruptcy Code or "arises in a case under" the Bankruptcy Code. *But see In re Harris,* 590 F.3d at 737-41.

Even so, Vickie Lynn Marshall's reading of § 157(b)(2)(C) sweeps too broadly and would permit the bankruptcy court to consider under § 157(b)(2)(C) counterclaims that are factually and legally unrelated to the claim being asserted against the bankruptcy estate. Such an expansive reading of § 157(b)(2)(C) would certainly run afoul of the Court's holding in *Marathon.*[28] It would also arguably be inconsistent with the Congress' intent to revise the Bankruptcy Code in a manner consistent with the principles of *Marathon* to make its jurisdictional grant constitutional.

Recognizing this shortcoming in her argument, and taking heed of our warning that the term "core proceeding" must be construed narrowly "to avoid potential constitutional problems arising from having Article I judges issue final orders in cases requiring an Article III judge," *Dunmore,* 358 F.3d at 1115, Vickie Lynn Marshall argues that her claim is a core proceeding arising in a case under the Bankruptcy Code because it is a *compulsory* counterclaim to the defamation claim asserted in Pierce Marshall's proof of claim and underlying his nondischargeability complaint. Vickie Lynn Marshall argues that the adjudication of a compulsory counterclaim effectively

[28] Indeed, most courts to have considered the issue have agreed that a limiting construction of § 157(b)(2)(C) is necessary to make it conform to the *Marathon* opinion. *See* Collier ¶ 3.02[3][d][i] (discussing the approaches that courts have taken to limit the broad sweep of § 157(b)(2)(C)).

becomes part of the claims allowance process, something that is unique and core to bankruptcy proceedings. She further argues that Pierce Marshall consented to the bankruptcy court's entering a final order on the counterclaim because it is a compulsory counterclaim to the proof of claim that Pierce Marshall chose to file with the bankruptcy court knowing that the proof of claim would be finally determined as a "core proceeding[ ] arising under title 11, or arising in a case under title 11." In support of these related arguments, she relies primarily on the Supreme Court case of *Katchen v. Landy,* 382 U.S. 323 (1966), and other cases that have discussed and reaffirmed *Katchen* after the passage of the 1984 Bankruptcy Amendments and Federal Judgeship Act. *See, e.g., Langenkamp v. Culp,* 498 U.S. 42, 44-45 (1990); *Granfinanciera v. Nordberg,* 492 U.S. 33, 57-60 (1989).

[5] We agree with Vickie Lynn Marshall that her claim is a compulsory counterclaim because the "operative facts underlying [her] action" are the same as those underlying the defamation claim. *See Pochiro v. Prudential Ins. Co.,* 827 F.2d 1246, 1250-51 (9th Cir. 1987) (applying Arizona law but relying on federal law in its analysis); *see* Fed. R. Civ. P. 13(a)(1) (defining a compulsory counterclaim as one held by the pleader at the time of service that "arises out of the transaction or occurrence that is the subject matter of the opposing party's claim" and "does not require adding another party over whom the court cannot acquire jurisdiction"). The defamation claim,

Vickie Lynn Marshall's affirmative defense of truth, and her counterclaim for tortious interference all concern the alleged efforts by Pierce Marshall to obtain control of his father's estate by inundating his father with estate planning paperwork and forging or otherwise improperly obtaining his father's signature on the document that made the Living Trust irrevocable.[29] Thus, under our "logical relationship" test, Vickie Lynn Marshall's claim qualifies as a compulsory counterclaim. *See Pochiro,* 827 F.3d at 1249-51.

We also agree with Vickie Lynn Marshall's second proposition-that a compulsory counterclaim, even one based entirely on state law, can be a "core proceeding[ ] . . . arising in a case under title 11." *Cf. In re Harris,* 590 F.3d at 738-41 (holding that a state law contract claim was a "core proceeding" that "arose under" title 11). We disagree, however, with her suggestion that *all* compulsory counterclaims

[29] Our review of the record reflects that Vickie Lynn Marshall had not joined the will contest until 1998, well after she had asserted the counterclaim in the bankruptcy proceeding. Thus the exception to compulsory counterclaims for those claims pending elsewhere, *see* Fed. R. Civ. P. 13(a)(2)(A), does not apply to the bankruptcy counterclaim. Furthermore, even if the claim had been pending in Texas, if the "defendant [here, Vickie Lynn Marshall] elects to interpose the pending claim as a counterclaim, . . . [s]he should be allowed to do so, and the counterclaim will be treated as if it were compulsory and thus under the ancillary jurisdiction of the court." 6 Wright & Miller, Federal Practice and Procedure § 1411 (citing, *inter alia, Union Paving Co. v. Downer Corp.*, 276 F.2d 468, 470 (9th Cir. 1960)).

must be "core proceedings . . . arising in a case under title 11." Instead, a closer consideration of the Supreme Court case upon which Vickie Lynn Marshall relies, *Katchen,* leads to the conclusion that some, but not all, compulsory counterclaims fall within the scope of § 157(b)(1) & (2)(C). Critical to the Court's decision that the bankruptcy court had jurisdiction over the trustee's counterclaim in *Katchen* was the fact that the bankruptcy court was unable to perform its statutory duty of allowing or disallowing the creditor's claim unless it ruled upon the trustee's counterclaim. *See* 382 U.S. at 329-30. According to the Court, ruling on the preference issue was "part and parcel of the allowance process," *id.* at 330, and "once the bankruptcy court has dealt with the preference issue nothing remains for adjudication in a plenary suit," *id.* at 334. Thus, the bankruptcy trustee's counterclaim had to be determined in order to rule upon the claims originally brought by the creditor against the estate. *See id.* at 330 (stating that the "bankruptcy court *must necessarily determine* "the voidable preference issue to resolve the creditor's claim against the estate) (emphasis added). That the Court also reasoned that a claimant "consents" to the court's jurisdiction of those matters which must be determined in order to resolve his claim, even if presented by way of a counterclaim, is an unsurprising conclusion.

There is no logical inconsistency to our holding that Vickie Lynn Marshall's counterclaim is compulsory but not "core." The test for compulsory

counterclaims is generous and designed to promote judicial efficiency by avoiding multiplicity of lawsuits. *See Albright v. Gates,* 362 F.2d 928, 929 (9th Cir. 1966). On the other hand, the standard delineating what is a core proceeding is much narrower because it is designed to comply with the constitutional limitations on the bankruptcy court's jurisdiction as set forth in *Marathon.*

[6] Our review of the evolution of the Bankruptcy Code, the Supreme Court's opinions in *Katchen* and *Marathon,* as well as our own jurisprudence cautioning against creating constitutional problems through an overly broad construction of what is a "core proceeding," *Piombo Corp. v. Castlerock Props. (In re Castlerock Props.),* 781 F.2d 159, 162 (9th Cir. 1986), leads us to agree with the amici curie [sic] professors that "a counterclaim under § 157(b)(2)(C) is properly a 'core' proceeding 'arising in a case under' the [Bankruptcy] Code only if the counterclaim is so closely related to the proof of claim that the resolution of the counterclaim is necessary to resolve the allowance or disallowance of the claim itself." Professors' Amicus Br. at 11. Such a construction of § 157(b)(2)(C) takes into account the whole of the statute, avoids rendering any terms superfluous, follows *Katchen,* and comports with the principles of *Marathon* and Congress' desire to revise the Bankruptcy Code in a manner consistent with the Constitution.

Vickie Lynn Marshall's compulsory counterclaim is not a core proceeding arising in a case under the Bankruptcy Code because it is not so closely related to Pierce Marshall's defamation claim that it must be resolved in order to determine the allowance or disallowance of his claim against her bankruptcy estate.

The district court correctly noted that "the nexus between the transactions out of which the claim and counterclaim arise . . . is somewhat attenuated," but its analysis went astray when it used a retrospective approach to support this factual finding. *In re Marshall,* 264 B.R. at 631 (stating that Pierce Marshall had obtained a judgment against Vickie Lynn Marshall's attorneys "*prior to the time* when his claim against Vickie was *ruled on by the bankruptcy court,*" making the main issue presented by Pierce Marshall's claim Vickie Lynn Marshall's responsibility for her attorneys' actions) (emphasis added).

[7] In bankruptcy cases, jurisdiction over a claim and the compulsory status of a counterclaim is determined as of the time the claim is pleaded. *In re Fietz,* 852 F.2d at 457 n.2. Accordingly, the analysis of whether a compulsory counterclaim such as Vickie Lynn Marshall's should be afforded "core treatment" must focus largely on what is available to the court at

the time of filing, that is, the parties' pleadings.[30] A review of Pierce Marshall's proof of claim and attached nondischargeability complaint and Vickie Lynn Marshall's answer, objections, and tortious interference counterclaim leads to the inescapable conclusion that the resolution of Vickie Lynn Marshall's counterclaim was not a necessary predicate to the bankruptcy court's decision to allow or disallow Pierce Marshall's defamation claim.

[8] The differences between the nature and scope of the factual allegations contained in Pierce Marshall's claim and Vickie Lynn Marshall's counterclaim support our conclusion that her counterclaim was not an integral part of the claims allowance and disallowance process. Pierce Marshall's defamation claim focused upon the alleged "tortious smear campaign" that Vickie Lynn Marshall and her attorneys devised "to obtain a quick recovery from the estate of J. Howard Marshall II." The statement at issue by one of the attorneys was that the attorney was:

[30] We say that the focus is largely on the pleadings because there may be other information available to the bankruptcy court, for example, by way of a motion under § 157(b)(3) or oral argument on the motion, that would not be retrospective in nature. *See* 28 U.S.C. § 157(b)(3) (providing that "[t]he bankruptcy judge shall determine, on the judge's own motion or on timely motion of a party, whether a proceeding is a core proceeding under this subsection or is a proceeding that is otherwise related to a case under title 11").

> "bothered" by "the blizzard of documents that were put in front of Howard Marshall to sign two weeks after his marriage to Anna Nicole Smith [Vickie Lynn Marshall]. . . . He signed all of them in almost completely illegible fashion which makes sense because he couldn't read at the time, according to his doctors. . . . J. Howard Marshall's signature appears as sort of a squiggle with only the 'J' clearly readable. . . . The documents, signed about two weeks after the oilman's June 27, 1994 marriage, gave the son full control over the J. Howard Marshall, II living trust. . . . The effect of it was basically an attempt to remove J. Howard Marshall from control of his estate."

Another statement by an attorney upon which Pierce Marshall based his claim was that "the law clearly entitles Smith [Vickie Lynn Marshall] to half of what her late husband earned during their marriage" and that there was some concern "about the documents [J. Howard] Marshall *purportedly* signed two weeks after his marriage." Pierce Marshall also found objectionable Vickie Lynn Marshall and her attorneys' efforts to tarnish his reputation by characterizing him as "greedy and miserly" and "a real control freak." Thus, Pierce Marshall's defamation claim and any defense of truth to such a claim would largely focus on whether J. Howard Marshall II had the capacity to sign the estate planning documents Pierce Marshall presented to him after J. Howard Marshall II's marriage to Vickie Lynn Marshall and whether he did, in fact, knowingly and validly execute the

documents. By way of comparison, the allegations upon which Vickie Lynn Marshall bases her tortious interference counterclaim are far less focused – they span a number of years, encompass various incidents of purported tortious conduct, and cover a broad array of financial and estate planning transactions beyond those which would be determinative of Pierce Marshall's defamation claim.[31] In addition to the differences in proof between the two claims, there is little overlap of the legal elements of the claims at issue. Pierce Marshall's defamation claim could be fully adjudicated without fully adjudicating Vickie

[31] For example, in her counterclaim Vickie Lynn Marshall made the following allegation:

> Debtor is informed and believes that Counter-defendant intentionally interfered with that expectancy by engaging in a concerted campaign to undermine Mrs. Marshall's rights and Mrs. Marshall's marriage to her Husband, by effectively imprisoning Mr. Marshall against his wishes, by surrounding Mr. Marshall with hired agents who reported to the Younger Son, by stationing armed guards to prevent access and personal contact between Husband and Wife, by cutting off support and obstructing the expressed wishes of Mr. Marshall, by deceiving Mr. Marshall, by attempting to undo gifts made by Mr. Marshall, by preparing documents and by ostensibly making transfers of property of Mr. Marshall which were inconsistent with his expressed wishes and desires, by making misrepresentations against Mrs. Marshall, by cutting off income to Mr. and Mrs. Marshall, by suborning false testimony against Mrs. Marshall, by abusing legal process, and by other actions that shall be proven at trial.

Lynn Marshall's tortious interference claim. Even if it were shown that the statements made by Vickie Lynn Marshall's attorneys were true (with the reasonable inference drawn from those statements being that Pierce Marshall used forgery or fraud to gain control of the Living Trust and make it irrevocable), in order to prevail on her claim, Vickie Lynn Marshall would still be obligated to establish, *inter alia,* that J. Howard Marshall II intended to make her an inter vivos gift, that it was reasonably certain that J. Howard Marshall II would have made the gift but for Pierce Marshall's inference, and the amount of damages that Pierce Marshall caused through his tortious conduct. Nothing in Pierce Marshall's defamation claim puts these factual and legal questions at issue.

In conclusion, although a compulsory counterclaim based on a state law cause of action can, under certain circumstances, be a core proceeding arising in a case under the Bankruptcy Code and be within the constitutional and statutory delegation of authority to bankruptcy judges to enter final orders, this is not such a case.

B

[9] Our conclusion that Vickie Lynn Marshall's counterclaim for tortious interference was not a "core proceeding[ ] . . . arising in a case under title 11" means that the Texas probate court issued the earliest final judgment on certain matters relevant to

this proceeding. Pierce Marshall argues that the district court erred when it refused to give any preclusive effect to the Texas probate court's judgment.[32] Having already noted in our previous opinion that "[o]ur review of the trial records in the Texas probate court and in the United States district court discloses conflicting findings of fact critical to the merits of the cases of the contesting parties," *In re*

[32] The district court denied Pierce Marshall's motion for summary judgment on the basis of res judicata and collateral estoppel. The district court reasoned that res judicata (claim preclusion) did not apply because Vickie Lynn Marshall did not actually litigate in Texas her claim against Pierce Marshall for tortious interference with an inter vivos gift. Nor did the district court believe that Vickie Lynn Marshall was obligated to bring the claim as a compulsory counterclaim because it was pending before the bankruptcy court when she joined the will contest in Texas. *See* Tex. R. Civ. P. 97 (excluding from the definition of compulsory counterclaim those claims that are "the subject of a pending action").

With respect to collateral estoppel (issue preclusion), the district court did not consider the Texas probate court's judgment to be final because the Texas probate court had plenary jurisdiction to change its judgment for a certain amount of time following its entry. The district court further denied the motion as untimely and inconsistent with the notion of fundamental fairness. Noting the motion was filed more than two years after the bankruptcy court's trial and after Vickie Lynn Marshall had nonsuited her affirmative claims in the Texas probate court, the district court also found that the identity of issues required for issue preclusion was lacking, explaining that "while it might be the province of the Texas probate court to determine what J. Howard intended to do with his estate when he died, the question before this Court is what he intended to do with it while he was still alive."

Marshall, 392 F.3d at 1123, it is perhaps unsurprising that we agree with Pierce Marshall that the doctrine of issue preclusion applies and that it prevents Vickie Lynn Marshall's success on her claim for tortious interference.

1

[10] Through the Full Faith and Credit Act, 28 U.S.C. § 1738, "Congress has specifically required all federal courts to give preclusive effect to state-court judgments whenever the courts of the State from which the judgment emerged would do so." *Allen v. McCurry,* 449 U.S. 90, 96 (1980). Under the doctrine of collateral estoppel, often called issue preclusion, "once a court has decided an issue of fact or law necessary to its judgment, that decision may preclude relitigation of the issue in a suit on a different cause of action involving a party to the first case." *Allen,* 449 U.S. at 94; *see also Robbins v. HNG Oil Co.,* 878 S.W.2d 351, 361 (Tex. App. 1994). To establish collateral estoppel under Texas law, a party must demonstrate: "(1) the facts sought to be litigated in the second action were fully and fairly litigated in the first action; (2) those facts were essential to the judgment in the first action; and (3) the parties were cast as adversaries in the first action." *Sysco Food Servs., Inc. v. Trapnell,* 890 S.W.2d 796, 801 (Tex. 1994). If these requirements are met, issue preclusion applies even when the subsequent litigation rests on a new theory of recovery. *Wilhite v. Adams,* 640 S.W.2d 875, 876 (Tex. 1982).

Under Texas law, an issue has been "fully and fairly litigated" if the particular fact or issue was the same in the two proceedings and was "actually litigated" in the prior proceeding. *See Nat'l Union Fire Ins. Co. v. Dominguez,* 793 S.W.2d 66, 71 (Tex. App. 1990), *rev'd on other grounds,* 873 S.W.2d 633, 637 (Tex. 1994). To determine if a matter was "actually litigated," Texas courts consider the following factors: "whether the parties were fully heard; whether the court supported its decision with reasoned opinion; and whether the decision was subject to appeal or was in fact reviewed on appeal." *Cole v. G.O. Assocs., Ltd.,* 847 S.W.2d 429, 431 (Tex. App. 1993).

2

The first step of our issue preclusion analysis is satisfied because several of the legal and factual issues that Vickie Lynn Marshall sought to litigate in the bankruptcy proceeding had already been litigated and finally determined in the Texas probate action.

[11] Under Texas law, a claim for tortious interference with an inter vivos gift arises when a person "by fraud, duress or other tortious means intentionally prevents another from receiving from a third person an inheritance or gift that [s]he would otherwise have received." Restatement Second of Torts § 774B; *see Marshall,* 547 U.S. at 311; *see also King v. Acker,* 725 S.W.2d 750, 754 (Tex. App. 1987) (discussing tortious interference with inheritance rights and citing the Restatement formulation of the

tort); *Brandes v. Rice Trust, Inc.*, 966 S.W.2d 144, 146-47 (Tex. App. 1998) (same). Such a person will be "subject to liability to the other for loss of the inheritance or gift." Restatement Second of Torts § 774B. As explained by the district court, the Texas courts have not clearly delineated the elements of a cause of action for tortious interference, but those jurisdictions which have generally agree that a plaintiff must prove (1) the existence of an expectancy, (2) a reasonable certainty that the expectancy would have been realized but for the interference, (3) intentional interference with that expectancy, (4) tortious conduct involved with the interference, and (5) damages. *In re Marshall,* 275 B.R. at 51 (citing *Dougherty* [sic] *(Doughty) v. Morris,* 871 P.2d 380 (N.M. 1994)). Vickie Lynn Marshall's ability to establish a number of these elements is compromised by the Texas probate court's factual findings.

[12] Most importantly, to prevail on her claim against Pierce Marshall, Vickie Lynn Marshall must prove that J. Howard Marshall II would have given her a substantial inter vivos gift but for Pierce Marshall's interference. This is contrary to the Texas probate court's finding that J. Howard Marshall II "did not intend to give and did not give to [Vickie Lynn Marshall] a gift or bequest from the Estate of [J. Howard Marshall II] or from the [Living Trust] either prior to or upon his death."

Vickie Lynn Marshall also has the burden of demonstrating that any interference by Pierce Marshall was tortious or, in the words of the

Restatement, that he used "fraud, duress or other tortious means" to prevent J. Howard Marshall II from giving Vickie Lynn Marshall the intended gift. To do so, Vickie Lynn Marshall primarily relied on Pierce Marshall's purported manipulation of his father's assets and his father's estate planning documents. The Texas probate court found, however, that the various estate planning documents executed by J. Howard Marshall were valid and reflected his desires. Specifically, the Texas probate court found that (1) J. Howard Marshall II's will and the 1982 Living Trust were valid, (2) J. Howard Marshall II had not been the victim of fraud or undue influence, and (3) J. Howard Marshall II possessed the requisite mental capacity when he executed the Living Trust, as amended, and his last will and testament. Also central to Vickie Lynn Marshall's ability to demonstrate a reasonable expectancy and ascertainable damages is the invalidation of the Living Trust. Vickie Lynn Marshall estimated that the value of her expected gift exceeded $300 million in her counterclaim; however, essentially all of J. Howard Marshall II's assets were held in the Living Trust after its creation in 1982. Shortly after his wedding to Vickie Lynn Marshall, J. Howard Marshall II modified his Living Trust to make it irrevocable. This modification, if valid, would prevent Vickie Lynn Marshall from ever being a beneficiary under the terms of the Living Trust, which is problematic to her claim of tortious interference because the very assets Vickie Lynn Marshall claimed that J. Howard Marshall II intended to give her were in the Living

Trust. The Texas probate court upheld the validity of the Living Trust, as amended, and found that it reflected J. Howard Marshall II's intended disposition of his property.

These issues were fully and fairly litigated by Vickie Lynn Marshall and Pierce Marshall in the Texas probate court. Vickie Lynn Marshall was a party to the Texas probate proceeding during all relevant times and was afforded ample opportunity to present her affirmative case (until she nonsuited her claims) and to defend against Pierce Marshall's counterclaim for a declaratory judgment. During the five-month trial in Texas, the jury and judge considered the evidence and arguments advanced by the parties, and the Texas probate court issued a reasoned opinion based upon the findings of fact as made by the unanimous jury.

The next step in our issue preclusion analysis is to consider whether the factual findings discussed above were essential to the Texas probate court's administration and final resolution of matters pertaining to J. Howard Marshall II's estate. Vickie Lynn Marshall argues that because she voluntarily nonsuited her claims in the Texas probate proceeding, the issues underlying her claims were not necessary to the Texas probate court's judgment. Although she opted not to pursue her claims for affirmative relief, Vickie Lynn Marshall remained in the probate proceeding as a defendant to Pierce Marshall's counterclaim. Pierce Marshall petitioned the probate court for a declaration that J. Howard Marshall II's

Living Trust and will reflected his true intentions and were valid. He further sought declaratory relief to determine Vickie Lynn Marshall's rights as to the estate and property of J. Howard Marshall II. Thus, Vickie Lynn Marshall was at all relevant times a party adverse to Pierce Marshall in the Texas probate court.

To decide Pierce Marshall's counterclaims for a declaratory judgment, the Texas probate court was obligated to discern J. Howard Marshall II's true intentions regarding the property held by the Living Trust. To do so, the court had to resolve allegations that J. Howard Marshall II's estate plan and the transactions underlying it were tainted by illegality and that, contrary to his estate plan, J. Howard Marshall II intended to give Vickie Lynn Marshall a substantial inter vivos gift. Thus, the Texas jury was tasked with responding to specific queries, many of which were on issues critical both to the resolution of Pierce Marshall's declaratory judgment request and to Vickie Lynn Marshall's success on her claim against Pierce Marshall for tortious interference with an expected inter vivos gift. The jury unanimously made the following factual findings: (1) the Living Trust and will were valid and had not been forged or altered, (2) J. Howard Marshall II had not been the victim of fraud or undue influence, (3) he had the requisite mental capacity when he executed his Living Trust and will, and (4) he did not have an agreement with Vickie Lynn Marshall that he would give her one-half of all his property.

The Texas probate court entered a final judgment in accordance with the jury's verdict and concluded that Pierce Marshall was entitled to his distribution as set forth in the Living Trust, as amended, and as provided in the last will and testament of J. Howard Marshall II.

The district court refused to give preclusive effect to any of the jury findings incorporated into the Texas probate court's judgment or to any of the Texas probate court's other factual findings or legal conclusions. Instead, the district court arrived at opposite findings on the same legal and factual questions.[33] In its 2002 judgment, the district court found that: J. Howard Marshall II intended to give Vickie Lynn Marshall a substantial gift that was to be in the form of a trust for her benefit; Pierce Marshall tortiously interfered with J. Howard Marshall II's intentions by engaging in illegitimate estate planning transactions; Pierce Marshall had altered the Living Trust to make it irrevocable in furtherance of his plan; and the Living Trust was invalid.

[13] The district court was not free to reach these contradictory findings of fact; instead, it was bound to afford preclusive effect to the relevant factual

[33] Notably, the district court made its factual findings without the benefit of the percipient witnesses that Pierce Marshall sought to have testify as part of his defense. The Texas probate court, however, held a five-month jury trial during which it took live testimony from the witnesses of all parties involved.

findings made by the Texas probate court. It was similarly bound to afford preclusive effect to the overlapping legal issues finally determined by the Texas probate court as a necessary step to the Texas probate court's determination of the validity of J. Howard Marshall II's estate planning measures.

[14] The final step in our issue preclusion analysis is to inquire whether the parties were cast as adversaries in the first action. There can be no doubt that this step is satisfied.[34] Before she nonsuited her claims, Vickie Lynn Marshall named Pierce Marshall as a defendant to many of her claims. After she nonsuited her claims, Pierce Marshall amended his claims to include a request that the district court enter a declaratory judgment with respect to Vickie Lynn Marshall's interest (or lack thereof) in the estate of J. Howard Marshall II and the Living Trust.

[15] All of the elements of issue preclusion have been met in this case. The district court erred when it did not afford preclusive effect to the relevant determinations by the Texas probate court. Had it done so, it would have concluded that various legal and factual issues necessary to establish Vickie Lynn Marshall's tortious interference claim had already

[34] It makes no difference to our issue preclusion analysis that in Texas, Pierce Marshall was named in his representative capacity, but in California, he was named in the counterclaim in his personal capacity.

been decided against her by the Texas probate court, such that Pierce Marshall was entitled to judgment as a matter of law.

IV

In conclusion, Vickie Lynn Marshall's counterclaim against Pierce Marshall for tortious interference with an inter vivos gift is not a "core proceeding[ ] arising under title 11, or arising in a case under title 11" for which the bankruptcy court is empowered to enter a final judgment. *See* 28 U.S.C. § 157(c). Because the Texas probate court's judgment was the earliest final judgment entered on matters relevant to this proceeding, the district court erred when it did not afford preclusive effect to the Texas probate court's determination of relevant legal and factual issues. Several of these determinations prevent Vickie Lynn Marshall from prevailing on her tortious interference claim in this proceeding. Because of our disposition of these two issues, we need not reach, and do not reach, the many other issues raised by Pierce Marshall and Vickie Lynn Marshall.

Neither party shall recover costs on the appellate proceedings subsequent to the Supreme Court's remand.

REVERSED AND REMANDED.

KLEINFELD, Circuit Judge, concurring:

I concur in the result reached by Judge Beezer's opinion. Vickie's counterclaim against Pierce is not a core proceeding, so the Texas probate court judgment preceded the district court judgment and controls.

I have no quarrel with the majority opinion, and offer no argument against it. I write merely to offer additional grounds that compel the same result.

Several alternative and independent grounds compel reversal: (1) because Pierce Marshall sought no damages from the bankruptcy estate, just a judgment that his Texas defamation judgment would not be discharged by the California bankruptcy, his claim could not affect the size of the estate available to Vickie Marshall's creditors; (2) Vickie's counterclaim for money could not affect whether Pierce's defamation claim was dischargeable; (3) Vickie's counterclaim was not related to the bankruptcy, because she had already been discharged and her creditors would get none of the money she sought from Pierce in her counterclaim; (4) Pierce's defamation claim in Texas was a common law claim for personal injury, which cannot be core. Vickie's counterclaim (itself a non-core tort claim) amounted to evasion of Pierce's constitutional right to jury trial in Texas. That evasion cannot stand shielded by bankruptcy court jurisdiction, especially when her bankruptcy was over and her debts discharged.

Pierce's proof of claim is attached to this concurrence as an appendix. He made two substantive entries on the form. For the date the debt was incurred he said "see attached Ex. 'A'. "And he checked the box for "unsecured nonpriority claim," and wrote "unliquidated" and "see attached Exhibit 'A'" rather than stating an amount. To understand what claim he made, we must therefore look at his exhibit A, which is attached.

Pierce's exhibit A is not a defamation claim for money. He had filed that in Texas years before, and was awaiting final judgment. Instead, exhibit A is entitled "complaint to determine dischargeability of debt pursuant to 11 U.S.C. § 523(a)(6)." Pierce alleges that Vickie and her lawyers defamed him in the press, in order to humiliate him and to extort a settlement from him of the claims against his father's estate. Their "willful and malicious acts," he alleges, "resulted in injury to the Plaintiff and/or the Plaintiff's property." But he does not seek money damages for this defamation. He was doing that in Texas. For his "cause of action" in bankruptcy court, Pierce pleads that "any discharge" Vickie may receive under bankruptcy law "will not discharge E. Pierce Marshall's claims against the Defendant." His prayer does not seek money damages, just a declaratory judgement "that the Plaintiff's claims against the defendant have not been discharged" and costs, attorneys fees, and such other relief as is just.

Vickie's counterclaim cannot be core because Pierce carefully framed his complaint to seek only a

declaratory judgment of nondischargeability, not a judgment that his defamation claim was meritorious and not a claim for money damages caused by the defamation. Bankruptcy court is the right place to litigate whether a debt was dischargeable. Pierce could not very well obtain judgment in a Texas trial court controlling dischargeability of a debt in a California bankruptcy. Bankruptcy court is the wrong place to litigate a common law claim for personal injury to final judgment, and Pierce did not seek to litigate his personal injury claim there.

The statute provides that "core" proceedings include "claims against the estate . . . but not the liquidation or estimation of contingent or unliquidated personal injury tort . . . claims against the estate for purposes of distribution in a case under chapter 11."[1] Thus "claim" for purposes of determining "core" is a statutory term of art meaning something narrower than what the word ordinarily means. Pierce's defamation claim would not be a "claim" under the statutory definition, because the statutory definition excludes unliquidated personal injury claims. Neither his defamation claim being litigated in Texas nor his nondischargeability claim filed in bankruptcy court would affect distribution of the estate. One might imagine, from the statutory language alone, that because Pierce's claim for a declaratory judgment of nondischargeability is core,

[1] 28 U.S.C. § 157(b)(2)(B); *see also id.* § 157(b)(2)(O).

that any counterclaim would be core.[2] But the cases construing the statute establish that such an interpretation would be mistaken.[3] Compulsory claims, such as setoff, can be core, but not all counterclaims are core.[4] Vickie's tort claim for interference with an expected gift, though a counterclaim to Pierce's claim for a declaratory judgment of nondischargeability of his defamation claim, is not core.[5] Were core

[2] *See id.* § 157(b)(2)(C) ("Core proceedings include, but are not limited to . . . counterclaims by the estate against persons filing claims against the estate").

[3] *See, e.g., Piombo Corp. v. Castlerock Properties (In re Castlerock Properties),* 781 F.2d 159, 162 (9th Cir. 1986) ("The apparent broad reading that can be given to § 157(b)(2) should be tempered by the *Marathon* decision.").

[4] *See, e.g., Dunmore v. United States,* 358 F.3d 1107, 1114 (9th Cir. 2004) (holding that non-core matters are those that "do not depend on the Bankruptcy Code for their existence and . . . could proceed in another forum"); *Sec. Farms v. Int'l Bhd. of Teamsters,* 124 F.3d 999, 1008 (9th Cir. 1997) ("Actions that do not depend on bankruptcy laws for their existence and that could proceed in another court are considered 'noncore.'"); *United States v. Yochum (In re Yochum),* 89 F.3d 661, 670 (9th Cir. 1996) ("In determining whether a matter is a non-core proceeding, we look to a variety of factors 'such as whether the rights involved exist independent of title 11, depend on state law for their resolution, existed prior to the filing of a bankruptcy petition, or were significantly affected by the filing of the bankruptcy case.'") (citation omitted).

[5] *See Wood v. Wood (In re Wood),* 825 F.2d 90, 97 (5th Cir. 1987) ("If the proceeding does not invoke a substantive right created by the federal bankruptcy law and is one that could exist outside of bankruptcy it is not a core proceeding; it may be related to the bankruptcy because of its potential effect, but . . . it is an 'otherwise related' or non-core proceeding.") (cited with

(Continued on following page)

jurisdiction over counterclaims read more broadly, *Marathon* would loom as a constitutional barrier.[6] The bankruptcy court had jurisdiction to make a determination of whether Pierce's claims against Vickie would survive bankruptcy because the question of whether a claim is dischargeable in bankruptcy involves "the restructuring of debtor-creditor relations, which is at the core of the federal bankruptcy power."[7] That determination, however, does not require adjudication of liability or damages on Pierce's or Vickie's tort claims, and that determination is all Pierce sought in bankruptcy court.[8]

approval by *Eastport Assocs. v. City of Los Angeles (In re Eastport Assocs.)*, 935 F.2d 1071, 1077 (9th Cir. 1991)).

[6] *N. Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 76 (1982) (plurality opinion) ("Art. III bars Congress from establishing legislative courts to exercise jurisdiction over all matters related to those arising under the bankruptcy laws. The establishment of such courts does not fall within any of the historically recognized situations in which the general principle of independent adjudication commanded by Art. III does not apply.").

[7] *Id.* at 72.

[8] *See Eastport Assocs.*, 935 F.2d at 1077 ("While the district courts have jurisdiction under 28 U.S.C. § 1334 to decide state claims if they are related to a bankruptcy case, the bankruptcy courts may only decide claims if they are part of core proceedings. In noncore proceedings, the bankruptcy courts may only make recommendations to the district courts. 28 U.S.C. § 157(c)(1).").

We held, applying *Marathon* and the 1984 Act implementing *Marathon,* in *Piombo Corp. v. Castlerock Properties (In re Castlerock Properties)*[9] that even though the debtor had filed a counterclaim to the creditors's claim, the counterclaim did not fall within the Bankruptcy Court's core jurisdiction. The creditor had not filed a claim for money in bankruptcy court, just for relief from the automatic stay, just as Pierce did not file a claim for money, merely for a nondischargeability determination. "In reaching this conclusion, we emphasized that courts 'should avoid characterizing a proceeding as 'core' if to do so would raise constitutional problems.'"[10] That, on its face, Vickie's counterclaim appears to fall within the words of § 157(b)(2)(C), does not, under *Castlerock* and *Marathon,* end the matter. The Supreme Court, in *Marathon,* held that "Congress may not vest in a non-Article III court the power to adjudicate, render final judgment, and issue binding orders in a traditional contract action arising under state law."[11] The same reasoning applies to Pierce's tort claim arising under state law, and Congress expressly

[9] 781 F.2d 159, 161 (9th Cir. 1986).

[10] *Taxel v. Elec. Sports Research (In re Cinematronics, Inc.),* 916 F.2d 1444, 1450 (9th Cir. 1990) (quoting *Castlerock,* 781 F.2d at 160).

[11] *Accord Thomas v. Union Carbide Agricultural Products Co.,* 473 U.S. 568, 584 (1985) (explaining the holding of *Marathon*).

preserved state law tort claims outside the jurisdiction of bankruptcy courts.[12]

Vickie's counterclaim is not related to the question of whether Pierce's defamation claim is dischargeable. Her tortious interference with a gift claim, if there is such a cause of action and she can prove its elements, could stand or fall regardless of whether his defamation claim was dischargeable or not. We need not reach the question whether, had Pierce sought damages for defamation as a creditor in bankruptcy, her counterclaim would be core, because he carefully avoided doing that. All that was required of the bankruptcy court in this case was to determine whether, if Pierce successfully proved in Texas what he pleaded in Texas, "willful and malicious injury" would preserve his judgment from discharge in Vickie's bankruptcy.[13] Whether a claim is dischargeable is a separate question from whether the claimant will prevail on the merits of that claim.[14] Because Pierce did not seek money from the bankruptcy estate for Vickie's defamation, or even estimation of the value of his claim,[15] Vickie's

[12] 28 U.S.C. § 157(b)(2)(B); *see also id.* § 157(b)(2)(O).

[13] 11 U.S.C. § 523(a)(6).

[14] *Grogan v. Garner,* 498 U.S. 279, 290 (1991) ("[N]ondischargeability [is] a question of federal law independent of the issue of the validity of the underlying claim.").

[15] 28 U.S.C. § 157(b)(2)(B).

counterclaim could not affect money distributable to her creditors and should not be deemed "core."[16]

Even if all the above analysis is mistaken, Vickie's counterclaim was not "core" for another independent reason. She had already obtained her discharge in bankruptcy. Her counterclaim could not enlarge the amount of money distributable to her creditors, because of the discharge. She sought money for herself only, not a nickel of which would be shared among her creditors. Her claim was only nominally "by her bankruptcy estate," and was in substance her personal claim for a judgment of hundreds of millions of dollars of which she would get every penny. Her claim should therefore be deemed not "related to" her bankruptcy case. My reasoning follows our holding in

[16] This is consistent with the Supreme Court's teachings in *Langenkamp v. Culp*, 498 U.S. 42 (1990), and *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33 (1989). In those cases, the outcome depended on whether the party claiming a jury trial had invoked the claims allowance process of the bankruptcy court by filing a claim against the estate. In *Granfinanciera*, the Court explained that because the petitioner had "not filed claims against the estate, [the trustee's] fraudulent conveyance action [did] not arise 'as part of the process of allowance and disallowance of claims.' Nor [was] that action integral to the restructuring of debtor-creditor relations. Congress therefore cannot divest petitioners of their Seventh Amendment right to a trial by jury." 492 U.S. at 58-59. In *Langenkamp* the parties claiming a right to jury trial had filed a claim against the estate, "thereby bringing themselves within the equitable jurisdiction of the Bankruptcy Court," and thus were not entitled to a jury trial. 498 U.S. at 45. Here, Pierce did not file a proof of claim seeking anything from the bankruptcy estate.

In re Fietz[17] that once a chapter 13 plan was confirmed, so that creditors could assert no interest in a subsequent recovery on a cross claim, the bankruptcy court lacked jurisdiction because the claim was not "related to" the bankruptcy case. Because the claim "could not have had any conceivable effect on administration of the bankruptcy estate" and would have been "beyond the reach" of the creditors, jurisdiction was absent.[18]

There is yet another independent reason, elementary and compelling even without the others, that the bankruptcy court was without jurisdiction over Vickie's counterclaim. Pursuant to the Bankruptcy Code, the bankruptcy court would not have had jurisdiction over Pierce's defamation claim even had he asserted it there, which he did not. 28 U.S.C.

[17] *Fietz v. Great W. Sav. (In re Fietz),* 852 F.2d 455, 457 (9th Cir. 1988) (holding that the standard for the bankruptcy court to exercise "related to" jurisdiction in an adversary proceeding is whether "the outcome of the proceeding could conceivably have any effect on the estate being administered in bankruptcy."); *Menk v. Lapaglia (In re Menk),* 241 B.R. 896, 907 (B.A.P. 9th Cir. 1999) ("Once the administration of the bankruptcy case has ended, the relation to the case becomes so attenuated that § 1334(b) 'related to' jurisdiction presumptively expires unless the court specifically retains jurisdiction.").

[18] *Fietz,* 852 F.2d at 459. *See also* the discussion of *Langenkamp* and *Granfinanciera* in footnote 16. Because Vickie's bankruptcy was discharged, Pierce's claim and Vickie's counterclaim no longer related to "the process of allowance and disallowance of claims" or were they "integral to the restructuring of debtor-creditor relations." *Granfinanciera,* 492 U.S. at 58-59.

§ 157(b)(5) requires that "the district court shall order that personal injury tort and wrongful death claims shall be tried in the district court." This statutory provision implements the holding in *Marathon* that Article III precludes bankruptcy courts from entering final judgments on tort claims founded on state law. Because bankruptcy judges cannot enter final judgment in such cases, they also "cannot try selected defenses in these tort cases. . . . The whole case, including defenses of all kinds, goes off to the district judge or the state court."[19] Pierce's defamation claim pending in Texas was for personal injury.[20] Vickie's claim, damages for tortious interference with a gift, was also a personal injury claim if it is a recognized tort.[21] Thus her claim is also outside the jurisdiction of the bankruptcy court. Accordingly, had Pierce filed a proof of claim for damages for defamation, the bankruptcy court would have lacked jurisdiction to enter final judgment on that claim. Because Vickie's counterclaim was a personal injury claim, be it in

[19] *Pettibone Corp. v. Easley*, 935 F.2d 120, 123 (7th Cir. 1991).

[20] *See In re Dillard Dept. Stores, Inc.*, 186 S.W.3d 514, 516 (Tex. 2006) (holding an employee's defamation claim fell within scope of an agreement requiring arbitration of claims for personal injuries); *see also Rizzo v. Passialis (In re Passialis)*, 292 B.R. 346, 348 (Bankr. N.D. Ill. 2003) (applying Texas law).

[21] *See Marshall v. Marshall*, 547 U.S. 293, 313 (2006) ("Texas courts have recognized a state-law tort action for interference with an expected inheritance or gift, modeled on the Restatement formulation."); *King v. Acker*, 725 S.W.2d 750, 754 (Tex. App. 1987) (discussing the availability of emotional distress damages under the Restatement (Second) of Torts § 774A (1977)).

defense of Pierce's defamation claim or an independent cause of action, the bankruptcy court would have lacked jurisdiction to enter final judgment on it.[22] Under *Marathon* and the statute, she could not evade Pierce's right to jury trial and an Article III court by shoehorning it into a bankruptcy filing, even had the discharge in bankruptcy not already rendered it not "related."

Pierce asserted a personal injury claim, defamation, in Texas, and prevailed in a five month jury trial in Texas. All he filed in Vickie's bankruptcy case was a claim for a declaratory judgment that whatever judgment he obtained in Texas would stand undischarged by Vickie's bankruptcy. Vickie used the vehicle of her bankruptcy case, even though it was effectively over, to file a personal injury claim against Pierce for interfering with a putative gift to her from his father. The bankruptcy court could not grant final judgment because her claim was for personal injury, was not related to the bankruptcy estate because she had obtained her discharge, and it was not "core." Pierce's constitutional rights to an Article III court and to jury trial as well as his statutory rights prevented jurisdiction in the bankruptcy court over Vickie's claim against him. When the bankruptcy court decided otherwise, it was without jurisdiction to do so.

[22] 28 U.S.C. § 157(b)(5).

APPENDIX

B10 (Official Form 10) - (Rev. 12/94) 1995 USBC, Central District of California

U.S. Bankruptcy Court, Central District of California

PROOF OF CLAIM

IN RE (Name of Debtor - if individual, enter Last, First, Middle)
VICKIE LYNN MARSHALL

Case Number
LA 96-12510 SB

NOTE: This form should not be used to make a claim for an administrative expense arising after the commencement of the case. A "request" of payment of an administrative expense may be filed pursuant to 11 U.S.C. § 503.

THIS SPACE FOR COURT USE ONLY

Name of Creditor
(The person or entity to whom the debtor owes money or property)
E. PIERCE MARSHALL

☐ Check box if you are aware that anyone else has filed a proof of claim relating to your claim. Attach copy of statement giving particulars.

☐ Check box if you have never received any notices from the bankruptcy court in this case.

☐ Check box if the address differs from the address on the envelope sent to you by the court.

Name and address where notices should be sent:
c/o John P. Melko
Verner, Liipfert, Berhard [sic],
McPherson and Hand
600 Travis, Suite 2600
Houston, TX 77002

Telephone No. (713) 225-7200

ACCOUNT OR OTHER NUMBER BY WHICH CREDITOR IDENTIFIES DEBTOR:

Check here if this claim:
☐ replaces
☐ amends

a previously filed claim, dated: JUN 12 1996

Ans'd

1. BASIS FOR CLAIM:

- ☐ Goods sold
- ☐ Services performed
- ☐ Money Loaned
- ☒ Personal injury/wrongful death
- ☐ Taxes
- ☐ Other (Describe briefly): _____
- ☐ Retiree benefits as defined in 11 U.S.C. § 1114(a)
- ☐ Wages, salaries, and compensations (Fill out below)
  Your social security number _____
  Unpaid compensation for services performed
  from _____ (date) to _____ (date)

2. Date Debt was incurred: see attached Ex. "A"

3. If Court Judgment, Date Obtained: N/A

4. CLASSIFICATION OF CLAIM. Under the Bankruptcy Code all claims are classified as one or more of the following: (1) Unsecured nonpriority, (2) Unsecured Priority, (3) Secured. It is possible for part of a claim to be in one category and part in another. CHECK THE APPROPRIATE BOX OR BOXES that best describe your claim and STATE THE AMOUNT OF THE CLAIM AT TIME CASE FILED.

☐ SECURED CLAIM $_____
Attach evidence of perfection of security interest
Brief Description of Collateral:

- ☐ Real Estate
- ☐ Motor Vehicle
- ☐ Other: _____

Amount of arrearage and other charges included in secured claim above, if any $_____

☒ UNSECURED NONPRIORITY CLAIM $ Unliquidated
A claim is unsecured if there is no collateral or lien on property of the debtor securing the claim or to the extent that the value of such property is less that the amount of the claim.

*see attached Exhibit "A"

☐ UNSECURED PRIORITY CLAIM $_____
Specify the priority of the claim.

- ☐ Wages, salaries, or commissions (up to $4000),* earned not more than 90 days before filing of the bankruptcy petition or cessation of the debtor's business, whichever is earlier) – 11 U.S.C. § 507(a)(3)
- ☐ Contributions to an employee benefit plan – 11 U.S.C. § 507(a)(4)
- ☐ Up to $1,800* of deposits toward purchase, lease, or rental of property or services for personal, family, or household use – 11 U.S.C. § 507(a)(6)
- ☐ Taxes or penalties of governmental units – 11 U.S.C. § 507(a)(8)
- ☐ Other – 11 U.S.C. § 507(a) _____

* Amounts are subject to adjustment on 4/1/96 and every 3 years thereafter with respect to cases commenced on or after the date of adjustment.

5. TOTAL AMOUNT OF CLAIM AT TIME CASE FILED:

$ Unliquidated	$ _____	$ _____	$ Unliquidated
(Unsecured)	(Secured)	(Priority)	(Total)

☐ Check this box if claim includes charges in addition to the principal amount of the claim. Attach itemized statement of all additional charges.

6. CREDITS AND SETOFFS. The amount of all payments on this claim has been credited and deducted for the purpose of making this proof of claim. In filing this claim, claimant has deducted all amounts that claimant owes to debtor.

THIS SPACE FOR COURT USE ONLY

7. SUPPORTING DOCUMENTS: *Attach copies of supporting documents*, such as promissory notes, purchase orders, invoices, itemized statements of running accounts, contracts, court judgments, or evidence of security interests. If the documents are not available, explain. If the documents are voluminous, attach a summary.

8. TIME-STAMPED COPY: To receive an acknowledgment of the filing of your claim, enclose a stamped, self-addressed envelope and copy of this proof of claim.

Date

6/11/96

Sign and print the name and title, if any, of the creditor or other person authorized to file this claim (attach copy of power of attorney, if any)

/s/ Joanne Mirras Knauss
Joanne Mirras Knauss, Attorney
for E. Pierce Marshall

Penalty for presenting fraudulent claim: Fine of up to $500,000 or imprisonment for up to 5 years, or both. 18 U.S.C. §§ 152 and 3571.

EXHIBIT A

Joanne Mirras Knauss (SBN #162655)
Rubinstein & Perry
355 South Grand Avenue
Thirty-First Floor
Los Angeles, California 30071
(213) 346-1000
(213) 680-3275 – Fax

John P. Melko
TBA No. 13919600
VERNER, LIIPFERT, BERNHARD
MCPHERSON AND HAND, CHARTERED
2600 Texas Commerce Tower
600 Travis
Houston, Texas 77002
(713) 237-9034
(713) 237-1216 (fax)

Attorneys for Plaintiff,
E. PEARCE [sic] MARSHALL

UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA
LOS ANGELES DIVISION

In re	§	Case No.
VICKIE LYNN MARSHALL,	§	LA 96-12510 SB
	§	Chapter 11
Debtor,	§	
	§	Adversary No.
E. Pierce Marshall,	§	96-01838
	§	
Plaintiff,	§	COMPLAINT TO
	§	DETERMINE
v.	§	DISCHARGE-
	§	ABILITY OF DEBT
Vickie Lynn Marshall	§	
	§	
Defendant	§	

§ PURSUANT TO 11
§ U.S.C. § 523(a)(6)
§
§ Status Con-
§ ference: 7/10/06
§ Time: 10:00 a.m.
§ Ctrm: 1575
§

TO THE HONORABLE UNITED STATES BANKRUPTCY JUDGE:

E. Pierce Marshall ("Plaintiff") files this Complaint to Determine Dischargeability of Debt Pursuant to 11 U.S.C. § 523(a)(6) against Vickie Lynn Marshall, A.K.A. Anna Nicole Smith "Defendant" and respectfully states as follows:

I. JURISDICTION

1. The Court has jurisdiction over this adversary proceeding under 28 U.S.C. §§ 1334(b) and 157(a). This adversary proceeding is a core proceeding under 28 U.S.C. §§ 157(b)(2)(J).

2. This adversary proceeding is commenced pursuant to 11 U.S.C. § 523 (a)(6) and Rule 7001(1) of the Federal Rules of Bankruptcy Procedure.

II. PARTIES

3. The Plaintiff is an individual and a resident of Dallas, Dallas County, Texas.

4. The Defendant is the individual debtor in the above-captioned Chapter 11 case. The Defendant may be served at 20 Ashdale Avenue, Los Angeles, California 90049 and/or through debtor's counsel. Joel B. Weinberg, Biegenzahn & Weinberg, 21031 Ventura Blvd., Suite 905, Woodland Hills, California 91364.

III. BACKGROUND FACTS

5. On August 4, 1995, J. Howard Marshall, II died. Immediately, his alleged widow, the Defendant, began seeking a settlement from the proceeds of J. Howard Marshall, II's estate. The Defendant and her attorneys, Diana Marshall and Suzanne P. Kornblit ("Kornblit"), instituted a plan to obtain a quick recovery from the estate of J. Howard Marshall, II by embarking on a tortuous smear campaign against E. Pierce Marshall and his family. The Defendant and her lawyers, Kornblit and Diana Marshall sought to humiliate and embarrass E. Pierce Marshall in an effort to get him to influence a settlement in favor of the Defendant and her attorneys from the estate of Plaintiff's deceased father. In their efforts to extort a swift settlement, the Defendant and her attorneys conspired to litigate their case in the press by making slanderous remarks and libelous statements with the intent that they would be published by the press. At the time each of these statements to the press was made, each individual knew that her statement was being recorded or transcribed for publication nationally.

6. After conducting this smear campaign for some time, the defendant and her attorneys briefly ceased their slanderous and libelous remarks to the press and demanded by written communication intended for E. Pierce Marshall that E. Pierce Marshall and representatives of the estate of J. Howard Marshall, II meet and discuss the allegations which the Defendant and her attorneys had made or else the Defendant and her attorneys would resume their campaign against E. Pierce Marshall.

7. Among other statements made to the press by the Defendant's attorneys in furtherance of this civil conspiracy, and in the course and scope of employment by the Defendant, was the statement by Diana Marshall to a reporter from the Houston Chronicle stating that Diana Marshall was "bothered" by "the blizzard of documents that week put in front of Howard Marshall to sign two weeks after his marriage to Anna Nicole Smith. . . . He signed all of them in an almost completely illegible fashion which makes sense because he couldn't read at the time, according to his doctors. . . . J. Howard Marshall's signature appears as sort of a squiggle with only the 'J' clearly readable. . . . The documents signed about two weeks after the oilman's June 27, 1994 marriage, gave the son full control over the J. Howard Marshall, II living trust . . . The effect of it was basically an attempt to remove Howard Marshall from control of his estate."

8. Diana Marshall spoke these defamatory words in the course and scope of her employment for

the Defendant. When Diana Marshall made these statements, she knew that the signatures of J. Howard Marshall, II were legitimate and were witnessed by several other persons. Diana Marshall knew that there was no evidence of any forgery, fraud or over-reaching by E. Pierce Marshall, but chose to make these false statements to the press anyway. She also neglected to tell the press about the other witnesses who were present at the time that J. Howard Marshall, II signed the documents. She also neglected to tell the press that the Defendant is alleging that J. Howard Marshall, II was capable of marrying the Defendant two weeks earlier and of understanding the implications of that act although Diana Marshall suggested in her defamatory comments that J. Howard Marshall, II lacked capacity to sign or did not sign the Trust documents. Despite her actual knowledge that her statements were false and defamatory, Diana Marshall made these statements and thereby committed libel and slander in furtherance of her employment by the Defendant.

9. The defamatory meaning of her statements is clear to any reasonable person. Diana Marshall intended the listener and/or reader of her statements to understand that her statements meant E. Pierce Marshall had used fraud and/or forgery wrongfully to steal control of the J. Howard Marshall, II living trust from his own father. Because the reasonable interpretation of her statements accuses E. Pierce Marshall of one or more criminal acts, Diana Marshall's statements constitute slander and libel *per se*.

The clear defamatory meaning of Diana Marshall's statements is illustrated by a newspaper account published by writer Vincent Lupo. In his account, Lupo stated: "Diana Marshall . . . told the Houston Chronicle recently that the law clearly entitles Smith to half of whatever her late husband earned during their marriage. The lawyer is more worried about the documents Marshall *purportedly* signed two weeks after his marriage to Smith. One of those documents gave the younger Marshall power of attorney over his father whose signature is a mere 'squiggle, with only the J clearly readable. . . .'" It is clear that Diana Marshall's statements taken as a whole were intended to convey either that the signatures were forged ("purportedly signed") or that the documents were signed by a man who was not capable of understanding them.

10. In further attempts to tarnish Plaintiff's reputation and in furtherance of her employment by Smith and the civil conspiracy by the defendants, Kornblit has made numerous defamatory statements to the press about E. Pierce Marshall. In one article, Kornblit characterized E. Pierce Marshall as "greedy and miserly." In another, Kornblit stated that the Defendant "forgives Pierce" and that "our side has always been cooperative . . . but we're just dealing with a real control freak on the other side." These defamatory personal attacks by Kornblit in furtherance of her employment by the Defendant and the civil conspiracy culminated in a letter meant for E. Pierce Marshall's eyes in which Kornblit threatens to

go back to the press if her demands for a meeting with E. Pierce Marshall and other interested parties were not met.

11. At all times relevant to this claim, Diana Marshall and Kornblit were working within the course of scope of their employment for the Defendant. The Defendant was informed of all activities by her attorneys and knew of the smear campaign that her attorneys were conducting in the press. The Defendant participated in the civil conspiracy in an effort to extort a speedy settlement.

12. The conduct described above further constitutes intentional infliction of severe emotional distress by the Defendant and her attorneys. As a proximate result of the Defendant's intentional conduct Plaintiff has suffered serious emotional distress, embarrassment and humiliation.

IV. CAUSE OF ACTION DETERMINATION OF DISCHARGEABILITY UNDER 11 U.S.C. § 523(a)(6)

13. The Plaintiff incorporates each of the above paragraphs by reference.

14. The Defendant is an individual debtor.

15. The Plaintiff's claims against the Defendant are claims arising from the Defendant's willful and malicious acts which resulted in injury to the Plaintiff and/or the Plaintiff's property.

16. Based on the foregoing, any discharge the Defendant may ultimately receive under 11 U.S.C. §§ 1141 or 727 will not discharge E. Pierce Marshall's claims against the Defendant.

WHEREFORE, the Plaintiff respectfully requests that the Court enter a judgment against the Defendant as follows:

1. A determination that the Plaintiff's claims against the Defendant have not been discharged;

2. An order granting the Plaintiff recovery for his reasonable costs and attorney's fees incurred herein and pre- and post-judgment interest as allowed by law; and

3. An order granting the Plaintiff such other relief as is just.

Respectfully submitted this 7 day of May, 1996.

RUBINSTEIN & PERRY

By: /s/ Joanne Mirras Knauss
Joanne Murras Knauss
355 South Grand Avenue
Thirty-First Floor
Los Angeles, California 30071
(213) 346-1000 – Phone
(213) 680-3275 – Fax

ATTORNEYS FOR E. PIERCE MARSHALL

PROOF OF SERVICE: By Mail
1013A(3) CCP Revised 5/1/88

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the County of Los Angeles, State of California, I am over the age of 18 and not a party to the within action; my business address is 355 S. Grand Avenue, 31st Floor, Los Angeles, California 90071.

On June 11, 1996, I served the foregoing document described as:

PROOF OF CLAIM

by placing true copies thereof enclosed in sealed envelopes addressed as follows:

John P. Melko, Esq.
VERNER, LIIPERT, BERNARD MCPHERSON AND HAND, CHARTERED
2600 Texas Commerce Tower
600 Travis
Houston, Texas 77002

Stephen F. Biegenzahn, Esq.
Joel B. Weinberg
Biegenzahn & Weinberg
21031 Ventura Blvd., Ste. 905
Woodland Hills, CA 91364

Office of the U.S. Trustee
Attn: Alvin Mar
221 N. Figueroa St., Ste. 800
Los Angeles, CA 90012

I am readily familiar with the firm's practice of collection and processing correspondence for mailing.

Under that practice it would be deposited with the U.S. Postal Service on that same day with postage thereon fully prepaid at Los Angeles, California, in the ordinary course of business. I am aware that on motion of the party served, service is presumed invalid if postal cancellation date or postage meter date is more than one day after date of deposit for mailing in affidavit.

Executed on June 11, 1996, at Los Angeles, California.

X I declare that I am employed by the office of a member of the bar of this court at whose direction the service was made.

CHRISTY BARRETT

275 B.R. 5

United States District Court,
C.D. California.
In re Vickie Lynn MARSHALL, Debtor.
E. Pierce Marshall, Plaintiff,
v.
Vickie Lynn Marshall, Defendant.
Vickie Lynn Marshall, Counterclaimant,
v.
E. Pierce Marshall, Counter-Defendant.
No. SA CV 01-97 DOC.
Bankruptcy No. LA 96-12510 SB.
Adversary No. AD 96-1838 SB.

March 7, 2002.

Rusty Hardin, Hardin & Associates, B. Lee Ware, Don Jackson, Ware, Snow, Fogel & Jackson, Houston, TX, Robert E. Mangels, Joseph A. Eisenberg, Herbert A. Bernhard, Julia J. Rider, Jeffer, Mangels, Butler & Marmaro, Los Angeles, CA, G. Eric Brunstad, Jr., Bingham, Dana, Hartford, CT, for E. Pierce Marshall.

Philip W. Boesch, Jr., Howard Stern, Boesch Law Group, Eric Berg, Zelle, Hofmann, Voelbel & Gette, Marina Del Rey, CA, Kent Richland, Sheila S. Kato, Greines, Martin, Stein & Richland, Los Angeles, CA, for Vickie Lynn Marshall.

FINDINGS OF FACT AND CONCLUSIONS OF LAW

CARTER, District Judge.

Before the Court is the proposed findings of fact and conclusions of law entered by the bankruptcy court in this matter on October 6, 2000 and November 21, 2000. Beginning on June 25, 2001, this Court conducted a de novo review of the bankruptcy court's proposed findings. From December 11, 2001 to January 8, 2002, this Court conducted an evidentiary hearing wherein it accepted the testimony of the central figures in the case, documentary evidence, and arguments of counsel. After reviewing all of the evidence in this matter, the Court adopts the findings of fact and conclusions of law of the bankruptcy court, with certain amendments, and makes independent findings of fact and conclusions of law, as set forth below.

PROCEDURAL HISTORY

Defendant and Counterclaimant Vickie Lynn Marshall (Vickie)[1] is the surviving widow of J. Howard Marshall, II (J. Howard), who died on August 4, 1995. Vickie, also known as Anna Nicole Smith, is a figure of some notoriety from her career as a model. J. Howard was also a figure of some notoriety as he was

[1] As all the principals in the matter at hand share the same last name, the Court will refer to the parties by their given names, as is customary in cases involving family members.

said to be either the richest or second-richest man in Texas at the time of his death.

The magnitude of the sums of money involved in J. Howard's estate has sparked intensely contested litigation on several fronts. First, succession proceedings[2] took place in Louisiana, but were dismissed in 1998 after the Louisiana Supreme Court found jurisdiction lacking in that state. *See In re Howard Marshall Charitable Remainder Annuity Trust,* 709 So.2d 662 (La.1998). Second, probate proceedings were commenced in Harris County, Texas. The case was tried to a jury and a verdict returned. Judgment was originally entered on August 15, 2001, with Amended Judgments entered on October 15, 2001 and December 7, 2001. Several motions for entry of an amended judgment were filed just before the judgment was to become final on January 7, 2002. On January 11, 2002, the Texas probate court denied those motions. Under Texas law, the judgment became final on February 11, 2002. On February 21, 2002, the bankruptcy court held that parts of the judgment in the Texas probate proceedings violated Vickie's discharge under the bankruptcy code, and was obtained only after J. Howard's youngest son, E. Pierce Marshall (Pierce) misrepresented to the bankruptcy court which claims he would pursue in the Texas Probate proceeding. *Marshall v. Marshall (In Re Marshall),* 273 B.R. 822 (Bankr.C.D.Cal.2002)

[2] Louisiana succession proceedings are similar to probate proceedings in most states.

(Marshall V). Third, on January 25, 1996, a few months after J. Howard's death, Vickie filed for Chapter 11 bankruptcy here in the Central District of California.[3] This bankruptcy case engendered two adversary proceedings with which this Court has had involvement.

In January 1998, Vickie filed an adversary complaint against Finley Hilliard as trustee of the J. Howard Marshall, II Living Trust and as executor of the succession of J. Howard Marshall, II. On July 22, 1998, the Honorable William D. Keller issued an order withdrawing the reference to the bankruptcy court of this proceeding, which thereafter proceeded before Judge Keller. On March 10, 1999, Judge Keller stayed the proceeding, pending the outcome of either the Texas probate proceedings or the present adversary proceeding, which is the subject of this order (the Adversary Proceeding). On November 2, 1999, the proceeding was transferred to this Court. That proceeding remains stayed.

The matter currently before the Court commenced on May 7, 1996, when Pierce filed an adversary complaint seeking a determination that Vickie owed him a debt that was nondischargeable. Pierce

[3] The bankruptcy court noted in one of its decisions that Vickie apparently filed for bankruptcy because, after not receiving an inheritance from J. Howard, she lacked money and also because a default judgment had been entered against her on claims brought by her former personal assistant or housekeeper. This claim subsequently settled.

alleged that Vickie had defamed him when, prior to the time she filed for bankruptcy and with her complicity, some of her lawyers told members of the press that Pierce had used forgery, fraud, and overreaching to gain control of J. Howard's assets.[4] On June 11, 1996, Pierce filed a proof of claim in the bankruptcy case. He made the claim by attaching a copy of the complaint from the adversary proceeding.

Vickie responded to both the adversary complaint and the proof of claim. On June 14, 1996, she answered the Adversary Proceeding complaint, asserting, in part, truth as a defense. She also asserted counterclaims for fraudulent transfer, an injunction, conversion, tortious interference, breach of fiduciary duty, abuse of process, fraud, promissory estoppel, breach of contract (third-party beneficiary), the imposition of a constructive trust, an accounting, and indemnity and contribution. As to Pierce's proof of claim, Vickie filed an objection on July 3, 1996.

After the case had gone through significant discovery disputes, Pierce filed a motion to withdraw the reference to the bankruptcy court of the Adversary Proceeding on September 22, 1998. That motion was assigned to Judge Keller for determination. Judge Keller issued a ruling on October 21, 1998

[4] Debts based on "willful and malicious injury," such as intentional torts, are not dischargeable. 11 U.S.C. § 523(a)(6). Damages for libel or defamation are not dischargeable when the statements were published with knowledge of their falsity. *Wheeler v. Laudani*, 783 F.2d 610, 615 (6th Cir.1986).

withdrawing the reference, but retaining the services of the bankruptcy judge for discovery purposes. On March 10, 1999, Judge Keller vacated the order withdrawing the reference, effectively returning this matter to the bankruptcy court.

On November 5, 1999, the bankruptcy court granted summary judgment for Vickie on Pierce's Adversary complaint. It found that Vickie had published no statements about Pierce, had not ratified any statements about Pierce made by her attorneys, and was not otherwise vicariously liable for any statements her attorneys had made about Pierce. Thus, the bankruptcy court held that Vickie had not committed a willful or malicious act under 11 U.S.C. § 523(a)(6).

Vickie's counterclaims against Pierce went to trial in the bankruptcy court in the fall of 1999. Approximately ten months later, on September 27, 2000, the bankruptcy court issued a Memorandum of Decision Following Trial (Original Decision). The Original Decision held that Pierce tortiously interfered with Vickie's expectation of the inheritance she otherwise would have received if she had exercised her right to a widow's election. On October 6, 2000, the bankruptcy court issued an Amended Memorandum of Decision Following Trial (Amended Decision), which superceded the Original Decision. *See Marshall v. Marshall (In re Marshall),* 253 B.R. 550 (Bankr.C.D.Cal.2000) *(Marshall I).* The Amended Decision concludes not that Pierce tortiously interfered with Vickie's expectation of an inheritance, but

that he interfered with her expectation of an *inter vivos* gift. *Id.* at 553. This was based, in large part, on facts found against Pierce as sanctions for discovery abuses, in addition to the evidence at trial. The bankruptcy court awarded Vickie $449,754,134 in damages. *Id.*

Pierce again filed a motion to withdraw the reference to the bankruptcy court. *See* 28 U.S.C. § 157(d). The case was randomly assigned to this Court for determination. On November 21, 2000, just prior to argument on that motion, the bankruptcy court issued a third order. This decision, the Supplemental Memorandum of Decision Following Trial (Supplemental Decision), does not supercede the Amended Decision, but instead supplements it by explaining that the bankruptcy court had determined that Vickie's counterclaims were core proceedings and by imposing punitive damages of $25 million.

This Court heard oral argument on Pierce's motion to withdraw the reference on December 11, 2000 and then took the matter under submission. The motion was later denied in this Court's Amended Order Regarding Subject Matter Jurisdiction. *See Marshall v. Marshall (In re Marshall),* 264 B.R. 609, 618 (C.D.Cal.2001) *(Marshall III).*

On December 29, 2000, the bankruptcy court entered a final judgment in this matter. *See Marshall v. Marshall (In re Marshall),* 257 B.R. 35 (Bankr.C.D.Cal.2000) *(Marshall II).* Pierce appealed that judgment to this Court.

In April 2001, this Court issued an Order Regarding Subject Matter Jurisdiction holding that the probate exception to federal jurisdiction did not apply, and therefore this Court did have subject matter jurisdiction, but finding that the matter was a non-core, "related to" matter pursuant to 28 U.S.C. § 157(c). Accordingly, the Court deemed the bankruptcy court's Amended Decision and Supplemental Decision as proposed findings of fact and conclusions of law pursuant to 28 U.S.C. § 157(c)(1) and began to undertake a de novo review of the record submitted in this matter. Both parties requested that the Court certify the matter for interlocutory appeal pursuant to 28 U.S.C. § 1292(b). On June 19, 2001, the Court entered an amended decision, certifying the matter for interlocutory appeal. *Marshall III*, 264 B.R. at 633. The parties filed cross-motions for leave to file an interlocutory appeal with the Ninth Circuit, which the Ninth Circuit denied.

On August 27, 2001, this Court held a status conference on the matter and set a schedule for hearing additional evidence. On October 5, 2001, this Court held a hearing on the evidentiary sanctions imposed against Pierce for discovery abuses. In a minute order of that date, the Court found that discovery abuses had taken place, but held in abeyance its decision on sanctions pending this order. In addition, the Court ordered Pierce to produce to Vickie in California several hundred boxes of documents previously withheld. On October 23, 2001, Pierce produced more than 400 boxes of documents to a document

repository stipulated to by the parties in El Segundo, California.

On November 2, 2001, Pierce filed a motion to dismiss or alternatively for summary judgment based on *res judicata*. The Court heard arguments on December 11, 2001 and on December 21, 2001, denied Pierce's motion. *Marshall v. Marshall (In re Marshall),* 271 B.R. 858 (C.D.Cal.2001) *(Marshall IV).*

Beginning on December 11, 2001, this Court heard evidence in the Adversary Proceeding. The Court heard live testimony from Harvey Sorensen, Edwin Hunter, Jeff Townsend, Vickie Lynn Marshall, and E. Pierce Marshall. The Court also reviewed numerous video and audio tapes, substantial documentary evidence not previously available, evidence and testimony offered by Pierce that the bankruptcy court had excluded as sanctions for Pierce's discovery abuses, and evidence adduced during the Texas probate proceedings. Additionally, the Court reviewed volumes of testimony from depositions and previous court proceedings submitted by the parties. On January 8, 2002, the Court heard argument of counsel and took the matter under submission.

SANCTIONS

A substantial portion of the findings proposed by the bankruptcy court were imposed against Pierce as sanctions for discovery abuses pursuant to Federal Rule of Bankruptcy Procedure 7037. *Marshall I,* 253 B.R. at 554 n. 5. On October 5, 2001, this Court heard

argument on the matter and held in abeyance its decision, pending a further showing of discovery abuse in light of the Court's order requiring the production of documents and a showing of prejudice by Vickie. After hearing evidence, the Court is able to make a determination of this matter on the merits and therefore does not reach the issue of evidentiary sanctions under Federal Rule of Civil Procedure 37(b)(2)(A). Therefore, except to the extent set forth in Footnote 17, the Court makes no findings on the issue of sanctions at this time.

FINDINGS OF FACT

I. THE LIFE OF J. HOWARD MARSHALL, II

J. Howard's autobiography, *Done in Oil,* harkens back to a nostalgic period in American history of allegedly self-made entrepreneurs who shaped our country. It recalls a time when the saying "go west young man" was the siren song for men and women of our country who left humble beginnings and crossed the rivers and plains to settle huge expanses of the nation. These ruggedly honest individuals walked the Oregon Trail, settled the Oklahoma territories, worked the California gold fields and inspired phrases like "Remember the Alamo," which needs no explanation to Americans. The myths and the reality of these individuals of character and vision survive and now form a large part of our country's history and folklore. J. Howard set himself in the context of these enterprising pioneers. Both parties have argued that to understand this case, the Court must

understand who J. Howard was and who Vickie is. At the outset, the Court admits to being uncomfortable with testimony that delved so intimately into their private lives. However, after a thorough review of the bankruptcy court's record and the testimony heard by this Court, the parties are correct to emphasize the particular nature of the individuals involved. The Court will therefore set forth some insights into the myths and reality of J. Howard and Vickie.

A. Background

Born in 1905, J. Howard attended private schools in the northeast part of the United States, including the George School, an exclusive New England prep school, Haverford College, an elite liberal arts college, and Yale Law School, one of the nation's leading law schools, from which he graduated *magna cum laude* in 1931. Although he often derided his undergraduate liberal arts education, he took great pride in the legal training he received at Yale. Upon graduation, he worked as an associate in a New York firm for two years. Subsequently he returned to Yale Law School to teach and later became the Assistant Dean.[5]

In the 1930's, J. Howard worked for the Roosevelt Administration on the proration of oil production.

[5] One of the subjects he taught at Yale was wills and trusts. Surely he did not realize at the time that these same subjects would take up large portions of his later life, and dominate his family's affairs for more than six years after his death.

During World War II he continued to work on petroleum supplies and logistics, serving on the government petroleum board.

After the War, J. Howard moved to Ashland, Kentucky and became president of Ashland Oil Company. He subsequently became Vice President of Mid-Continent and by the mid 1950's he was working for Signal Oil in California. In 1954, J. Howard was one of the founders of Great Northern Oil and Gas Company. The initial stockholders were Woodley Petroleum, Southern Production, Sylvester Dysone and J. Howard. The wealth of the Marshall family is primarily based on the interest acquired by J. Howard in Great Northern Oil and Gas, the predecessor company to Koch Industries.

B. First Marriage

J. Howard met and married his first wife, Eleanor Pierce Marshall (Eleanor)[6] in the 1930's. Their marriage produced two children, J. Howard Marshall, III (J. Howard, III) and Pierce.

Eleanor has been described to the Court as a refined, gentile, spiritual, and religious woman. In her sixties, well after her divorce from J. Howard, Eleanor became a minister. Now ninety-seven years old, the Court was told the story that when she was being deposed in one of these related matters, she

[6] Eleanor later re-married and is now Eleanor Stevens.

inquired of counsel how long the deposition would last, because she did not want to miss her dancing lessons later that day. Eleanor was the primary caregiver for Pierce and his older brother due to the absenteeism of J. Howard as he pursued his business ventures.

The older brother, J. Howard, III, has been described to the Court as a true scholar. He attended Cal Tech and graduated at the top of his class. J. Howard, III formed a company in Los Angeles immediately following graduation and has remained a southern California resident throughout his lifetime. J. Howard was immensely proud of J. Howard Marshall, III but disinherited him over a financial disagreement involving the buy-back of Koch stock, *see* Part I.D, *infra*.

Pierce attended a military academy in Indiana and Webb School in Claremont, California. Subsequently he attended Pomona College, graduating in 1961. Following graduation he worked briefly in Michigan and then served in the Navy from 1963-65. He married in 1965 and he and his wife have been married for over thirty-five years. Pierce worked in California and New York as an investment banker until he moved to Texas in 1968 at the urging of his father. J. Howard wanted Pierce to become involved in oil and gas ventures. Neither Pierce nor J. Howard Marshall, III had spent much time with their father while growing up and the significant bond between Pierce and J. Howard seems to have developed during Pierce's years in Texas working with his father.

Throughout the remainder of the 1960's and 1970's Pierce and J. Howard invested together in businesses which ranged from oil and gas to restaurant ownership.

In 1961, the thirty-year marriage between Eleanor and J. Howard dissolved. J. Howard was fifty-five years old at the time of the divorce, and at that time, two trusts were created to hold J. Howard's and Eleanor's now separate property interests. Trust B was formed on behalf of Eleanor and Trust S on behalf of J. Howard. However, Eleanor left her financial affairs in the hands of her former husband because she trusted his business acumen.

C. Second Marriage

In December 1961, J. Howard married Betty Bohannon Marshall (Betty). At his father's request, Pierce served as the best man. There are no children from this marriage.

Betty and J. Howard had met in the mid-1930's. She has been described to the Court as strong, intelligent, street smart, astute in business, and a good match for J. Howard. J. Howard Marshall, III always believed that his father had a long-term relationship with Betty during his marriage to Eleanor.

In 1961, J. Howard accepted the Presidency of Union Texas and he and Betty moved to Houston. When most people are planning for retirement, J.

Howard was continuing the pursuit of the business that had been the focus of his life.

J. Howard created what he referred to as a "new community" for he and Betty. Although not formalized until years later, to J. Howard, this new community always existed. It consisted of any assets that he and Betty acquired during their marriage, even if they could be traced back to his own separate property.

In the early 1980's Betty was diagnosed with Alzheimer's disease. Her condition slowly deteriorated until her death in the Fall of 1991.

D. Koch Industries and the Disinheritance of J. Howard, III

Koch Industries (Koch) is a privately held, integrated petroleum and chemical conglomerate headquartered in Wichita, Kansas. Koch is estimated to be the second largest privately held company in the United States based on revenues of approximately $35 billion dollars. Koch Industries is unique among privately held companies in that it pays out a low dividend and instead reinvests its funds in order to grow the company. To that end, Koch Industries has been an unqualified success, growing at dramatic rates over the last two decades.

Koch's history can be traced back to Great Northern Oil and Gas company, which formed in 1954 with J. Howard owning 16%, Southern owning 40%,

Woodley owning 40% and the remaining percentages owned by minority shareholders. Subsequently, Fred Koch purchased Southern's 40% interest in Great Northern. Woodley eventually sold its interest to Pure which subsequently sold to Union Oil. Union Oil then sought to take over Great Northern, and merge it into Union Oil, making it a publicly traded company. J. Howard and the Koch family prevented the takeover.

Fred Koch and J. Howard shared the same ideas about business. Their belief was that earnings should be reinvested in the company to create sustained growth. They also believed their company should be privately held. To them, the management advantages of a privately held company outweighed short-term benefits of going public and making a quick profit in the public market. They wanted to be able to make quick business decisions without being encumbered with the need for shareholder approval, which was time consuming and often divisive. They also did not want to be subject to yearly shareholder demands for high dividend returns. This private business philosophy has been steadfastly adhered to for decades.

The Koch family eventually bought out Union Oil's interest and changed the name to Koch Industries. Fred Koch chose his son Charles Koch to take over as president of Koch Industries. J. Howard promised Fred Koch that he would always support Charles Koch and support keeping Koch Industries a privately held company. Since the late-1960's, Charles Koch has been Chairman and CEO of Koch

Industries. On his death, Fred Koch left equal shares of his voting stock in Koch Industries to his four sons, Charles, David, Bill, and Fred Jr. (Freddie).

In 1974, J. Howard Marshall, III wed in Los Angeles. At the reception J. Howard gave each of his sons 4% of the voting common stock. Although legally he would have no voting rights, J. Howard believed he could still control this 8% minority voting right through J. Howard, III and Pierce. Upon giving his sons the stock, J. Howard said: "Boys, these are the Crown Jewels, take care of them."

A disagreement erupted in 1980 between the children of Fred Koch about the future of Koch Industries. Bill and Freddie Koch believed that the best approach was to go public. Charles and David Koch, however, knew that their father would want the company to stay private. A fight for control of the family business ensued.

Freddie and Bill and their allies could count 48% ownership in the company, just short of the majority that they would need to install a new board that would approve a public offering. To find the extra votes, they looked outside the family. Freddie and Bill approached Pierce, now the owner of 4% of the voting stock, and asked him to vote with them, but he declined. However, when Bill and Freddie approached J. Howard, III, he sided with them, giving them the votes needed to oust the old board, including J. Howard. As far as J. Howard, III was concerned, it was time to go public.

When J. Howard heard about this, he felt betrayed. J. Howard had shared the vision of a privately held company and its virtues with Fred and Charles Koch. It can be safely said that he believed that J. Howard, III should never go against the family. J. Howard flew to California to try to change his son's position, but was unable to convince him. J. Howard then made J. Howard, III an offer to buy back the stock for $208 per share, a total of $8 million.

J. Howard took this action despite the fact that he viewed the purchase price as exorbitant. The previous highest transaction for Koch stock had been $80 per share between Koch and its employees. J. Howard felt that he had been forced to pay a premium to obtain this stock from his own son.

Because the dividends could not cover the financing for the $8 million transaction, J. Howard sold the stock back to the company. He had honored his commitment to his friend, the late Fred Koch, but it would have immediate consequences within his own family. J. Howard flew back to Houston and disinherited his eldest son. He considered the $8 million payment an early inheritance and planned to give him nothing more.

With J. Howard's faction firmly in control again, Koch Industries resolved to stay private. At Charles Koch's urging, Koch Industries bought out the stock of the dissident shareholders. The effect of this buyout was that the remaining shareholders' ownership interest nearly doubled. The Koch family (primarily

Charles and David Koch) now own more than 80% of Koch's common stock and 88% of its voting stock. The buyout, however, would engender more troubles. Led by Bill and Freddie Koch, the dissident shareholders sued Charles and David Koch, J. Howard, Pierce, and the remaining Koch shareholders. They contended that the price that they received in the buy-out was far below the true value of Koch Industries. Major litigation over billions of dollars commenced.

Charles Koch stated publicly and in sworn testimony that there are no present plans to go public. The Court accepts these representations. His father was dedicated to maintaining Koch as a privately held company and Charles Koch has remained steadfast in adhering to this goal. Market conditions may eventually force this company to go public, possibly to pay estate taxes. But as of this date, the longevity of this commitment to remain a private company, the lengthy and factious family dispute between Charles Koch and other family members who wanted to take the company public, and Charles Koch's testimony convinces the Court that going public is not a pending or planned event.

Due to the dispute over Koch's true value, reducing the apparent value of Koch Industries became an important goal for Koch shareholders, including Pierce and J. Howard.

E. J. Howard's New Estate Planning

In 1982, J. Howard embarked on an estate plan to make certain that the Koch stock would never be held hostage. His eldest son was completely excluded as an heir. A comparison of his 1979 will with his 1982 will demonstrates his intent to exclude his eldest son and leave Betty, and upon her death, Pierce, as his heirs. (Ex. 3203.) From 1984, Pierce was the ultimate beneficiary of J. Howard's estate. J. Howard employed attorney Harvey Sorensen to represent him and the various entities he created for his estate plan. He also asked Pierce to assist Sorensen in the creation of these entities.

On July 1, 1984, the company known as Marshall Petroleum, Inc. (MPI) was formed by J. Howard, Betty, and Eleanor in a Section 351 tax-free exchange of property for stock. MPI's assets comprised the separate property of J. Howard from Trust S, the separate property of Eleanor from Trust B, and Betty's share of her and J. Howard's "new community." In May of 1991, the company elected S-Corporation status.

At its formation, J. Howard owned 56% of MPI, Eleanor owned 37%, and Betty owned 7%. In 1989, Eleanor decided that she wanted to increase her charitable giving. She then established a Charitable Remainder Trust, with Pierce as the ultimate beneficiary, and sold a portion of her MPI stock back to the company for cash. In 1991, Betty died and her ownership passed to J. Howard and subsequently to Pierce.

Over this time period, Pierce bought stock in MPI and received stock as compensation for his consulting services. By 1992, the ownership changes resulted in J. Howard controlling approximately 70% of MPI.

The main asset of MPI was J. Howard's Koch stock. Upon forming MPI, J. Howard transferred to MPI his Koch stockholdings. Although he hoped that MPI would become an active oil and gas company in its own right, and indeed for some time it was involved in various oil and gas deals, its only real purpose by the time J. Howard died was as a holding company for Koch stock. Through the veil of a corporation, J. Howard sought to protect his Koch stock, and pass it on to Pierce while avoiding as much estate tax consequences as possible.

The evidence reflects the number of Koch shares that MPI held. The Texas Commerce Bank required collateral for a line of credit for MPI. The presentations to the Texas Commerce Bank Loan and Discount Committee, which were made while J. Howard was alive, state that J. Howard, through MPI, owned 862,535 shares of Koch stock. (Ex. 685.) The same documents indicate that MPI had pledged 505,885 shares to Texas Commerce Bank as collateral. Koch issued and had outstanding 5,850,908 shares of common stock. The 1995 Presentation lists J. Howard's percentage ownership as 14.7% based on his ownership of 862,535 shares of the 5,850,908 shares of Koch common stock as of December 31, 1994. (Ex. 685.)

The 1995 and 1996 Credit Approval Presentations state that "the bank does not receive financial statements on Marshall Petroleum and thus the dividend income that MPI receives from Koch stock is relied upon for repayment of bank debt. The Company [MPI] received dividend income of $8MM and $7MM in 1995 and 1994, respectively." The report notes that as a privately held company, access to Koch's audited financial statement is limited and that historically the bank received updates of Koch's financial performance from Pierce. (Exs.684, 685.)

F. J. Howard's Affair with Lady Walker

In 1982, J. Howard met "Lady" Diane Walker. Feeling the need for a drink after a day at the office, he went to a "strip joint, a titty bar" as he described it in his videotaped deposition in 1992. (Ex. 3225.) Lady Walker was one of the strippers who took everything off for J. Howard in return for his generous dollar bills. Thus, at the age of seventy-eight, he began his pursuit of Lady Walker.

J. Howard wanted Lady Walker to be his exclusive mistress and he often professed his desire and commitment to marry her if Betty died. Money was immediately bestowed upon her. The intensity of his pursuit is set forth in his letters to her.

These letters contain repetitive and aggressive protestations of his love, always coupled with a

reference to money.[7] "Jungle Money" and "Pin" are code words for money that J. Howard gave to Lady Walker. "Pin" was a regular payment made on a consistent and timely basis,[8] "Jungle money" was a payment for her own pleasure,[9] and "big kills" were larger sums given sporadically to Lady Walker.[10] J. Howard also gave Lady Walker enormous amounts of jewelry, including more than $1 million purchased from Harry Winston and Nieman Marcus, the same stores at which he would subsequently buy jewelry for Vickie.

At one point, J. Howard sent Lady Walker the Koch Industries prospectus in an apparent attempt to

[7] "Light of my life/ . . . Now, as always you can count on/my love and devotion – our 'Jun'/money is but a small sample of my concern for my lady – . . . " (Ex. 630, p. HBOM 0015501.)

" . . . my proposal to beg you to be my mistress." (Ex. 630, p. HBOM 0015502.)

"Dear Lady – /I fear I am a nuisance – I still hope I am a beloved nuisance – of course/I shall do what you ask 'stop calling' . . . it is part of the juice of my devotion . . . All of this is a far, far cry from the years gone by . . . you said I could 'call you/whenever I wanted.' I fear I have abused it. If so, it is only because I love you . . . " (Ex. 630, p. HBOM 0015505.)

[8] "Dear Lady – /Perhaps true love never/runs smooth – but since I love you truly, this 'pin'/ tries to tell you I am/Your devoted man" (Ex. 630, p. HBOM, 0015479.)

[9] "Lady love: /Jungle & Pin" (Ex. 630, p. HBOM 0015481.)

"My Lady Love – /Increased Jungle Money – /+/Pin/+/Sharom" (Ex. 630, p. HBOM 0015483.)

[10] "Another 'pin' to go with/Big Kill" (Ex. 630, p. HBOM 0015486, H-108-1480.)

impress her with his wealth. The front of the first page reads, "For Lady – /The Crown jewels/ J. Howard." (Ex. 630.)

This pattern of giving money, and even the terms that J. Howard used, is the same pattern that Vickie describes of J. Howard's pursuit of her a decade later. Lavish jewelry, regular payments of money, and sporadic gifts ushered these bar dancers into J. Howard's life. Apparently, it was extremely lucrative to have an affair with J. Howard. J. Howard spent approximately $2 million a year on Lady Walker, which is approximately the same amount of money he spent each year on Vickie when he pursued her a decade later.

J. Howard's statement that "men in love do stupid things and I was sure guilty" is accurate. (Ex. 3225.) In J. Howard's case, it was a consistent pattern.

G. The Death of Betty Marshall and Lady Walker and the Beginning of the Lady Walker Litigation

J. Howard's affair with Lady Walker continued uninterrupted until she died suddenly as a result of complications from facelift surgery on July 9, 1991 at the age of fifty-one. The effect of her death on J. Howard was initially described by him as the most tragic thing that ever happened to him. Ironically, shortly after Lady Walker's death, J. Howard discovered that she had betrayed their relationship and

had been living with another, much younger, man during most of their affair. Outrage drove J. Howard to sue her estate in January 1992 seeking the return of almost $15,000,000 in gifts that J. Howard had given Lady Walker (the Walker Litigation). J. Howard accused Lady Walker of fraud, claiming she received kickbacks from merchants after the items were purchased and the merchants had charged J. Howard's account. Because J. Howard hated lawyers and disliked handling details, he appointed Pierce to deal with the details of the matter.

H. IRS Gift Tax Audits

In 1989, J. Howard's gifts to Lady Walker came to the attention of J. Howard's attorney Harvey Sorensen. Sorensen, a tax specialist, became concerned. J. Howard had never filed gift tax returns on the gifts, nor had he indicated any particular concern with doing so. J. Howard's position with respect to the gift taxes was largely similar to his position with estate taxes – he did not want to pay them and it was his lawyers' job to figure out how to avoid them.

Sorensen, however, understood that the gifts were subject to a gift tax that had gone unpaid, and knew that this avoidance of the tax laws would cause substantial interest and penalties from the Internal Revenue Service. Sorensen eventually determined that between $12 and $14 million was given to Lady Walker without taxes being paid. In 1989, he filed amended tax returns for the years 1983-87. These

eventually caused the IRS to audit J. Howard and initiate tax collection proceedings.

J. Howard repeatedly attempted to avoid taxes, and during the gift tax litigation, it was discovered that he had, in fact, found a way to use his affair with Lady Walker to his advantage. In the gift tax litigation, J. Howard took the unlikely position that his "pin" payments to Lady Walker were consulting fees. At one point, he suggested that she received a salary of $1 million per year to handle his public relation work. He not only tried to escape gift taxes this way, but it is likely that he deducted his payments to Lady Walker from his income tax returns.

His efforts to hide gifts in the guise of legitimate business operations were disclosed in the testimony of his closest advisors. Jeff Townsend testified that Finley Hilliard, J. Howard's accountant, told Townsend that J. Howard wanted to funnel funds to Lady Walker. Two corporations were formed, in part as a way for J. Howard to give Lady Walker money. Stock of Coliseum, Inc. was held in trust for her benefit and he gave her gifts of Presidio, Inc. stock. Lady Walker also served on the MPI Board of Directors. When questioned about her functions, he replied, "I guess she was a Director – never active – she never undertook anything as a Director." (Ex. 3225.)

In 1993, Sorensen was relieved of his responsibilities of representing J. Howard, after more than ten years of service. Pierce contends that the reason Sorensen was terminated was because he was not

aggressive enough in the disputes with the IRS. However, this contradicts the characterization of J. Howard being fiercely loyal to his employees, who were in turn loyal to him. Sorensen was eventually replaced as J. Howard's lead tax counsel and estate planning lawyer by Edwin Hunter, whose approach to tax litigation was far more aggressive, and whose actions on behalf of Pierce Marshall have become the focal point of the present case.

J. Howard, his family, estate, and MPI became mired in numerous disputes with the IRS. Once again, J. Howard would call on Pierce to handle the details of the litigation. These disputes focused on two critical issues: (1) gifts given by J. Howard to his paramours and (2) the valuation of MPI, and therefore Koch, stock. Once again, the legion of lawyers working on behalf of J. Howard, his estate, and later Pierce, were faced with the quandary of the defending the valuation of MPI and Koch stock.[11]

Reducing the value of Koch and MPI stock had become the central organizing principle of J. Howard's legal team. There was no other goal. They sought to make J. Howard, who was considered one of the 400 richest men in the world and the wealthiest in the

[11] Disputes over gift tax and inheritance tax liability between J. Howard's estate and the IRS are still pending, and the IRS has agreed to keep a settlement offer open until this Court's proceedings are completed. The IRS may want to take a closer look at the summaries written on J. Howard's personal account, and passed on to his accountant, for illegitimate tax deductions.

state of Texas, appear to be holding as his primary asset a minority interest in a company that had very little market value, despite being one of the largest and most successful oil conglomerates in the country. Failure to do so would cost J. Howard millions of dollars in disputes with the IRS.

Koch valuation was just as important to Pierce, who personally owned Koch voting stock, making him a party to the Koch valuation litigation. He also stood to inherit J. Howard's Koch interest and the valuation problems inherent in these tax disputes with the IRS.

I. Summary

It is fair to say that J. Howard was an immensely successful businessman. He served on boards of numerous corporations and banks and became involved with a number of oil and gas ventures in Texas. J. Howard was also heavily involved in Koch Industries, as described herein. J. Howard's success earned him a ranking in Forbes Magazine as one of the 400 wealthiest men in America, and the wealthiest man in Texas. But the rating rankled J. Howard, and he claimed to dislike the publicity that it brought. What worried J. Howard more than publicity was the spotlight that it shined on his wealth. Being named as one of the richest men in the country was likely to attract the attention of the IRS.

J. Howard was a well-trained lawyer. Oddly, however, he did not appear to have much regard for

the profession. He was reputed to dislike lawyers and the details of lawyering. To his mind, a legal document should never be more than one page long.[12]

J. Howard is also described as being irascible and demanding. Perhaps to those who knew him, those personality traits were endearing. To outsiders, he was viewed simply as impatient and hostile. His tendency to bang the table to make his point was viewed as being in command of a situation. However, the Court's view is that, at least late in his life, J. Howard's theatrics were transparent.

In addition, J. Howard's disregard for the tax codes was a pattern he followed his entire life. For ninety years, he showed nothing but contempt for the IRS and the tax codes of this country. Throughout his life he surrounded himself with excellent legal counsel who were creative in attempting to circumvent the tax codes.[13] He ignored gift taxes until he could no longer evade the issue. He railed against the inheritance tax provisions, claiming that being forced to pay estate and income taxes was "double taxation," while at the same time he avoided paying substantial income taxes by: writing off as business expenses the

[12] It is ironic then that his death has created the largest volume of legal filings in the history of the Southern Division of Central District of California.

[13] Surprisingly, much what J. Howard managed to do was within the confines of the law, allowing him to evade taxes by stepping through loopholes that only someone of his great wealth could afford to find.

gifts to his paramours Lady Walker and Vickie, whom he claimed were consultants; financing his lifestyle by taking a line of credit against his valuable stock holdings, the proceeds of which are not taxable income; and hiding and manipulating his assets in aggressive accounting gimmicks.

In summary, this court is not impressed with the character of a man who had the finest private school and legal education and who consciously avoided the very taxes that millions of American families comply with every year. It is in the collection of these taxes that the government must rely on the good faith and honesty of our citizens to fund our nation's needs in time of peace and war. The fact that J. Howard could not see fit to comply with these laws, despite the great advantages that he was afforded by American society, speaks poorly of his character.

II. VICKIE LYNN MARSHALL

Vickie dreamed of becoming the personification of her idol, Marilyn Monroe. Both became international superstars, traveling far from home under assumed names. Norma Jean's fame thrust her into the arms of an American baseball icon and a dashing young politician, while Vickie Lynn found herself in the company of a Texas oil baron. But her notoriety never reached the same heights or longevity. Her life is best described as that of a person who was rescued by her wealthy pursuer and taught to spend money at a breathtaking pace that most Americans cannot

fathom. While she detested being thought of as a gold-digger, her actions leave little doubt that money was the central facet of her relationship with J. Howard. Her appetite for money, once developed, was incessant and outlandish by everyday standards.

Vickie appeared before the Court to testify for three days. Her communication skills were poor as she frequently had trouble engaging counsel. Her illiteracy is striking. Examples are too numerous to chronicle but include writing "25.00" meaning $2,500 and "4500,00" meaning $4,500 – she testified that she has trouble with zeros. In fact, she has only recently started learning to pay her own bills after years of managers and relatives managing her money. Vickie also finds herself in difficult times and is being treated for depression.

But education is no guarantor of integrity and a discredited profession does not mean a person lacks truthfulness. While Vickie certainly drew a more noble image of herself than the facts bear out, her testimony on the statements made by J. Howard are credible.

A. Background

Vickie Lynn Marshall was born in Houston, Texas in 1967. Her parents divorced shortly after she was born and her father moved away. She never saw him until she looked him up after she had become Playmate of the Year. In her teens she moved with her mother to Mexia, Texas, a small town in the

eastern part of the state. She completed grade school, but failed her freshman year in high school, and never progressed past an eighth grade education.

Vickie worked as a waitress and morning cook at Krispy Fried Chicken in Mexia where she met Billy Wade Smith, who was the cook at the restaurant. At the age of 17, she married Billy Smith, and at the age of 19, she gave birth to her son Daniel, her only child. The marriage ended shortly thereafter, and Vickie moved back to Houston with Daniel when he was a year old.

B. Career as a Dancer

At this point in her life, Vickie was estranged from her family. Her husband, Billy Wade Smith was not providing child support and made no effort to visit Daniel. Initially she found employment at Walmart and later as a waitress at the Red Lobster, but she could not make enough money to support herself and Daniel. Vickie testified that one day, while on the way home from work, she passed a neon sign that displayed a lady in high heels wearing a bikini. She was interested in becoming a dancer, but deferred at first when she found out it was a nude dance bar. She initially sought a job as a waitress but was quickly talked into dancing on stage. After a couple of drinks, humiliated but willing to dance, she overcame her inhibitions and continued as a dancer when she saw "all the money in her lap which paid the bills."

Vickie, however, was big-boned, and in the fashion trends of the late 1980's and early 1990's, her figure relegated her to the "B" team. Instead of working the lucrative night shifts, Vickie danced during the day, for less pay and fewer tips. But this apparent disadvantage would soon work in her favor.

III. J. HOWARD'S AND VICKIE'S TIME TOGETHER

J. Howard and Vickie began their relationship in October 1991, when they met at Gigi's in Houston, Texas. They married June 27, 1994 and their relationship continued until his death on August 4, 1995. They met when she was at the vibrant age of twenty-four, and he a sickly eighty-six year-old man. The issues of J. Howard's donative intent and Vickie's expectancy can only be understood by slowly unwinding their years together.

A. The Meeting of J. Howard and Vickie

After Lady Walker and Betty died in 1991, J. Howard entered a period of deep despondency. He appeared to his family and friends to have lost his zest for life. In 1991, J. Howard told his eldest son, J. Howard, III, that "he enjoyed having pretty women on his arm when he entered the River Oaks Country Club in Houston and that a great light had gone out of his life."

In October 1991, Vickie was dancing at Gigi's, a Houston strip club. Dan Manning was J. Howard's

driver who frequented Gigi's and had seen Vickie dance. Manning and J. Howard had talked about going to a burlesque bar and in October, Manning drove his boss to Gigi's to cheer him up. Because of J. Howard's age and physical condition, he did not go out at night, and thus they arrived during the day-shift, when Vickie worked. Manning approached Vickie and asked her to dance for J. Howard. According to Vickie, when she saw J. Howard, "he looked terrible, he looked like he had lost his will to live." While Vickie danced, J. Howard tried to grab her breasts. Thus began J. Howard's aggressive pursuit of Vickie's affection. He asked [ ] her to have lunch with him the next day. A description of this lunch helps to understand the pattern that they followed for the years of courtship prior to their marriage.

B. The Courtship

J. Howard initially took Vickie to a restaurant hotel and ordered room service. He told Vickie about Betty and Lady Walker and funny stories about himself. When she became concerned about her job, he gave her an envelope with a thousand dollars in cash and told her not to go to work. The following day they had lunch at River Oaks Country Club, where once again she was given cash. On each occasion, money was given to her ranging in amounts of $1,000 to $5,000 in cash. Vickie "stopped dancing right after Howard met me that day." (Dep. of Vickie, Dec. 28, 1999, vol. 3, p. 600.) J. Howard was soon paying all of Vickie's bills. Shortly after they met, J. Howard

purchased a white Toyota Celica as a gift for her after her own car had been repossessed.

She started receiving $2,000 checks twice a month. (Ex. 48.) These checks were recorded by J. Howard's assistant Eyvonne Scurlock for consulting, just as his previous "pins" to Lady Walker had been. Summaries prepared by Scurlock were then sent to J. Howard's accountant for tax purposes and 1099 Tax forms for Vickie were prepared. (AP 11462, Dep. of Eyvonne Scurlock, August 27, 1999. pp. 72, 576-577.) These $2,000 checks increased over time to $2,750.

Within a week of their meeting, J. Howard told Vickie that he was going to marry her. He had been re-invigorated by Vickie. While he had fallen into a state of deep despair after the deaths of Lady Walker and Betty, his relationship with Vickie brought him back to life. He called her "the light of his life." He told his attorney Harvey Sorensen numerous times that he wanted to marry Vickie.

According to Vickie, J. Howard asked her to marry him "tons of times." She contends that the proposals were usually accompanied by the same assurance that once they were married, she would have half of everything he had. His proposals occurred frequently, and are confirmed by numerous friends, employees and professional associates. He started buying her rings that increased in size and value. When he gave her rings, there was always the same conversation about marriage. "It seemed like every time he would buy me a bigger and bigger ring

and he would ask me over and over and over and he was very pushy. He really loved me. He just really wanted to marry me." (Dep. of Vickie, December 28, 1999, p. 642.) During J. Howard's courtship of Vickie, he purchased at least three large engagement rings as well as numerous smaller rings. On each occasion, the giving of these rings was accompanied by the same incessant matrimonial proposals.

J. Howard's aggressive pursuit is illustrated by one instance where he purchased jewelry for Vickie from Nieman Marcus. On Christmas Eve 1993, David Watson, a Nieman Marcus employee, delivered various pieces of jewelry to Vickie's home for her and J. Howard to review. Vickie looked at all the pieces, and commented that a particular yellow diamond ring was too expensive and should not be shown to J. Howard. When J. Howard arrived, he looked at the jewelry and commented: "this is better than the Home Shopping Network." J. Howard then asked if he had seen everything. Watson, forgetting Vickie's admonition, showed J. Howard the yellow diamond ring. When told that the price was, $107,000, J. Howard stated: "Oh, just a baquetta." J. Howard then completed the purchase. That purchase, and an earlier one by J. Howard in April 1993, were the two largest purchases in store history.

During their courtship, J. Howard made numerous other gifts to Vickie. On September 16, 1992, J. Howard purchased a ranch for Vickie in Tomball, Texas, outside of Houston (the Tomball Ranch). This ranch was purchased in the name of the J. Howard

Marshall, II, Living Trust (the Living Trust), but was intended for Vickie's use and benefit. J. Howard later purchased a home on Rusington Street in Houston, which was held by the Houston Land Trust, with her as the beneficiary. J. Howard also rented the Los Angeles house that Marilyn Monroe had lived in. When the lease expired, he purchased a house on Ashdale street in the Brentwood area of Los Angeles for her. J. Howard also provided Vickie with an apartment in New York City when she spent time there. He bought her $10,000 gowns that could only be worn once because in "Hollywood you could never wear the same dress twice." Jewelry purchases from Harry Winston jewelers for Vickie exceeded $2 million. In 1992, J. Howard purchased a new Mercedes Benz for Vickie.

Vickie testified that J. Howard taught her to spend money, and that spending money was fun. She was the second of two women with little wealth and no experience whom J. Howard taught that there were no limits to the fun of spending money if they were with him.

J. Howard eventually introduced Vickie to Pierce. On one occasion in 1992, J. Howard took Vickie and Pierce to lunch at the Royal Oaks Country Club. From the outset, the relationship between Vickie and Pierce was tense. Vickie already believed that Pierce did not like her, and felt that during the entire lunch he was giving her "mean looks." According to Vickie, when J. Howard went to the restroom, Pierce told her "don't let J. Howard buy you anything else."

J. Howard nevertheless repeatedly proposed to Vickie. She had just started taking voice and modeling lessons when she met J. Howard, and although she was flattered by these proposals, she wanted to have a career first. Vickie put off J. Howard almost three years before she finally accepted his proposals.

Shortly after they met, Vickie saw an ad in the newspaper to audition for *Playboy Magazine.* After meeting with a scout, Vickie was quickly hired and two weeks later was doing a test shoot in California. In March 1992, Vickie made her *Playboy* debut, appearing on the cover. In May 1992, she was named *Playboy* Playmate of the Month.

Vickie was contacted by Guess Jeans to be part of its national advertising campaign. She became their top spokes-model for a one-year period from 1993-94. During this time, she appeared in numerous other magazines and in 1993 was named the *Playboy* Playmate of the Year. Vickie had achieved the level of international sex symbol, and was one of the most recognized print models in the world. Her stardom only encouraged J. Howard to pursue her with a newfound vigor.

In Spring 1994, Vickie was on tour for Guess Jeans in Singapore. While there, she and the Guess Jeans entourage were mobbed by fans. The incident scared her, and the remainder of the tour stops in Japan and the Philippines were cancelled. When she returned home to Houston, J. Howard once again proposed to her. J. Howard repeated that she was the

woman who had saved his life, that he would take care of her and her son, and that she would have half of everything he had. This time, Vickie accepted.

Vickie testified that his money was a factor in her decision to marry J. Howard, but contends that she would have married him anyway. Vickie sought security for her and her son, and what he might lack in youth, vigor, and looks, J. Howard made up for with his great wealth. Although she has often been portrayed to the Court as a gold-digger and predator, she did hold a certain regard for J. Howard, and was willing to compromise her prime modeling years for someone who showered her with gifts and offered financial security.

C. The Marriage of J. Howard and Vickie

J. Howard and Vickie were married on June 27, 1994 at the White Dove Wedding Chapel in Houston, Texas. Although numerous prenuptial agreements had been prepared, beginning as early as 1992, none were signed, nor was any such agreement ever discussed with Vickie.

The wedding was not widely announced, and Pierce did not learn of the wedding until after it occurred. Only a few close confidantes attended, including J. Howard's assistant Eyvonne Scurlock, his new driver Arnold Wyche, his nurse Charlotte Fade, and Vickie's aunt and uncle, Elaine and Melvin Tabers. Henry Schlesinger, one of the MPI executives was invited, but did not attend.

The night of the marriage, Vickie flew to New York on an assignment, leaving J. Howard in Texas. On July 6, 1994, J. Howard left for California to visit his new wife.

During their marriage, J. Howard continued to give extravagant gifts to Vickie. J. Howard also considered adopting Vickie's son Daniel. One of J. Howard's lawyers, Jeff Townsend began seriously investigating the issue. He contacted counsel in California about possible adoption proceedings and traveled to California to meet with attorney Lawrence Leone. (Ex. 143.) The adoption, however, never took place because Townsend determined that he would not be able to obtain consent from Daniel's natural father, Billy Wade Smith. The steps taken to begin an adoption proceeding demonstrate that J. Howard was prepared to undertake a greater commitment to Vickie and her son, not only during his lifetime, but long afterward.

Vickie and J. Howard also tried to have children of their own. Initially, they tried to have children in what Vickie described as "the normal way." When that did not work, J. Howard went to a fertility doctor to seek advice and treatment.

D. Post-nuptial estate planning changes

After J. Howard and Vickie were married, J. Howard's estate plan changed. Although his will was not changed at that time, the Living Trust was amended to become irrevocable. His interest in MPI

was reduced until, by summer of 1995, he was stripped of all of his ownership interest in the company. These changes were made by a series of documents that are the heart of the claims of tortious interference, *infra*.[14]

E. Illness and Death of J. Howard

J. Howard traveled to Los Angeles in December 1994 to spend Christmas and New Year's with Vickie and Daniel. He and Vickie had, until that time, kept their relationship out of the public spotlight. They planned to make their relationship public at the New Year's Eve party at the *Playboy* Mansion in Beverly Hills.

J. Howard was overjoyed. His joy at being with Vickie is demonstrated by pictures of him with Vickie that Christmas. (Ex. 264.) Although Vickie appeared to have a pleasant Christmas Day, she spent most of the rest of the time J. Howard was visiting hidden away in her separate bedroom.

[14] The primary documents that changed J. Howard's estate plan are, *inter alia*: the Grantor Retained Annuity Trust (GRAT) of August 1993; the sale of MPI stock to Pierce in exchange for a promissory note in August 1993 (the Pierce Note); the Amended and Restated Living Trust of July 13, 1994; the Assignment of the Pierce Note, purportedly dated June 1, 1994; the Promissory Note between J. Howard and MPI, purportedly dated June 1, 1994; the Pledge of Pierce Note to MPI, purportedly dated June 1, 1994; the Renunciation of Income Distribution from the Living Trust; the Donation of the GRAT to the Living Trust; and the Sale for Private Annuity of MPI stock.

After Christmas, J. Howard fell ill and returned to Houston, where he planned on picking up his tuxedo and seeing his doctor before returning to Los Angeles in time to attend the New Year's Eve party with Vickie. However, J. Howard's illness turned out to be pneumonia and he was hospitalized at the Park Plaza Hospital on January 1, 1995.

J. Howard returned home after his release from the hospital on January 13, 1995 but he never regained his good health. On January 23, 1995, Vickie returned to Houston from Los Angeles and found J. Howard in a deplorable state. She stayed up with him that night, and she and his nurse Charlotte Fade fed him chicken soup. Sometime in the early morning hours, J. Howard choked and his heart stopped. CPR was administered and J. Howard was rushed to the Spring Branch Hospital, where he stayed until February 9, 1995.

After this near-death experience, Vickie's dispute with Pierce began in earnest. Pierce had left instructions that J. Howard was not to be suctioned and Vickie was infuriated. She believed that Pierce had decided to let his father die. During J. Howard's stay in the hospital, Pierce refused to pay for her bills or give her any additional money. On February 4, 1995, Vickie went to Spring Branch Hospital at 2 a.m. to visit J. Howard. She brought along a friend of hers, Raymond Martino, a Hollywood producer. Martino videotaped Vickie and J. Howard together, presumably so that Vickie could use the tape in court – either of law or of public opinion. On another occasion,

Vickie brought a tape recorder and sought to tape J. Howard. She climbed into his bed, exposed her breasts and asked J. Howard: "Do you miss your rosebuds?" (Testimony of Letisha Hunt, Tr. of Tex. Probate Trial, Feb. 21, 2001, pp. 18-19.)

During this time, it was clear that J. Howard was dying. His attorney Jeff Townsend began making funeral arrangements and trying to determine who would take charge of J. Howard's body. (Ex. 650, p. 21929.)[15] On February 22, 1995, J. Howard again returned to Park Plaza Hospital, where he stayed until March 30, 1995. While there, J. Howard underwent gall bladder surgery. In the Spring of 1995, unbeknownst to Vickie, J. Howard was diagnosed with inoperable, terminal stomach cancer.

As his health deteriorated, the dispute between Vickie and Pierce intensified. Pierce believed that Vickie's bills were excessive and directed that all of Vickie's creditors contact her directly. He stopped paying for her expenses. Vickie sued in state court in Harris County, Texas for spousal support.[16] That

[15] Townsend's research proved prescient. The odiousness of the parties involved in this case was displayed when Pierce sought to have J. Howard cremated, while Vickie insisted he be buried in California. The Texas probate judge, seeking the wisdom of Solomon, ordered that the ashes be divided between Pierce and Vickie. *See* 1 Kings 3:16-28 (King James). Pierce and Vickie each took their half of J. Howard's remains.

[16] During this time period, Vickie had hundreds of thousands of dollars in her checking account.

litigation was soon followed by guardianship proceedings, where Vickie and Pierce both sought to be appointed guardian of the person of the ailing J. Howard. When J. Howard returned home, Pierce hired off-duty Houston police officers to guard J. Howard at his home. Although Pierce testified that these guards were hired only to insure J. Howard's safety, they appeared in situations where there was no danger of harm. Vickie was not allowed to visit J. Howard without the guards being present. Glenn Johnson, who the Texas probate court had appointed temporary guardian ad litem for J. Howard, testified that he too was not allowed to visit J. Howard without the presence of the guards. Johnson testified that the guards were intimidating and opined that they had been hired to prevent Vickie from visiting J. Howard. He believed that Vickie, who was in Houston frequently during June and July of 1995, wanted to see J. Howard more often, but would not go to J. Howard's home because of the guards. Pierce had reason to keep Vickie from seeing J. Howard, because, as detailed, *infra,* he was concerned that she might be able to get him to sign a new will or gift instrument.

Nevertheless, from April through July, Vickie visited or telephoned J. Howard on a nearly daily basis. Vickie's visits decreased in July 1995, when she spent some time in the hospital herself. On August 4, 1995, J. Howard died at the age of 90. He was survived by his two sons, his wife, and an unprecedented volume of litigation.

In sum, their lives were intertwined in need, driven by greed and lust. Nevertheless, the Court is convinced of his love for her. J. Howard referred to Vickie as the "light of my life," and the lady that saved his life. His relationship with her provided the happiest moments of his last few years. He considered Vickie his reason for living, and the joy that she brought him undoubtedly helped him live another four years. There is no question that he showered her with gifts, that he sought to protect her and provide for her.

The Court is more cautious about her love for him. J. Howard became Vickie's knight in shining armor. His help propelled her to the highest levels of stardom, something unimaginable for a girl from her background. She cherished the protection and security that he afforded her and the lavish gifts that he gave to her in order to win her affection. J. Howard used his money to get Vickie to fall in love with him, and in her own way, Vickie loved J. Howard.

IV. TORTIOUS INTERFERENCE

A. J. Howard's Donative Intent

Upon meeting Vickie, J. Howard immediately began bestowing numerous gifts upon her. As detailed *supra,* J. Howard gave Vickie millions of dollars worth of gifts in the form of cash, property, cars, and jewelry. Besides these gifts, however, the evidence demonstrates that J. Howard intended to give Vickie

a gift that would provide for her once her modeling career was over and he had passed on.

In the fall of 1992, J. Howard's estate planning lawyer Harvey Sorensen began preparing for J. Howard's goal of wedding Vickie. At J. Howard's direction, he drafted a pre-nuptial agreement for J. Howard and Vickie. This agreement was presented to J. Howard on November 18, 1992. The draft pre-nuptial agreement was 58 pages. (Ex. 3242.) The draft agreement provided that Vickie would receive certain amounts of money upon the termination of the marriage by either death or divorce. Vickie was to receive $100,000 for each month that J. Howard and Vickie were married. Vickie was also to get an additional $5 million if she and J. Howard had a child together. Largely as a result of J. Howard's lingering bitterness from Lady Walker's betrayal, J. Howard insisted that the draft agreement include a provision that if Vickie had intercourse with anyone other than J. Howard during their marriage, that her payment would be reduced by half. (Ex. 3342.)

J. Howard believed the draft agreement was too long. He insisted that legal documents be only one or two pages and he directed Sorensen to revise the agreement. But from this time forward, J. Howard adhered to his plan to make a substantial gift to Vickie. One of his last recorded statements is a tape recorded message to the Texas probate judge on May 26, 1995, where he states: "I want my wife [Vickie] to be supported by me." (Ex. 364.)

During this same time period, J. Howard turned to attorneys Edwin Hunter and Jeff Townsend, both of Lake Charles, Louisiana. He gave Hunter the draft pre-nuptial agreement that Sorensen had prepared and asked Hunter to prepare a new pre-nuptial agreement that was not so long. At this point, he set Townsend and Hunter to work on a parallel path as Sorensen.

At the same time, J. Howard was seeking other avenues to give gifts to Vickie. J. Howard directed Townsend and Hunter to prepare documents for a "Marshall Farms" corporation to run the Tomball Ranch that he had purchased for Vickie. (Ex. 58.) Additionally, he asked Hunter and Townsend to prepare documents for a "corporation for Vicky's [sic] business." (Ex. 58.) Through this, J. Howard intended to buy Vickie numerous gifts of clothing and jewelry that would help her develop her career and image in Hollywood. In order to make the corporation not appear to be a sham to the IRS, Vickie would sign an agreement for the corporation to have rights to exploit her celebrity image through goods such as perfume and clothing, in exchange for salary from the corporation, another gift to Vickie. Vickie was to eventually receive the proceeds from these goods.

Finally, J. Howard directed Hunter and Townsend to draft a "catch-all" trust for Vickie. (Ex. 58.) As described, *infra,* this draft trust instrument was never produced to the Court. However, the circumstances under which it was drafted lead the Court to the inescapable conclusion that the "catch-all" trust

was intended to be a document whereby J. Howard would transfer assets to Vickie, to be held in trust for her until after his death.[17]

On December 14, 1992, J. Howard and Townsend spoke about the plans for Vickie. Townsend primarily specialized in gas and oil leases, but was a confidant to J. Howard, and fulfilled many roles. The next day, he sent a letter to his colleague Hunter. It memorialized his conversation, and asked for a progress report. (Ex. 58.) It detailed the four things that J. Howard wanted done: a pre-nuptial agreement, the Marshall Farm corporation, the corporation for Vickie's business, and a "catch all trust." (Ex. 58.) Townsend's letter was a reminder to Hunter to get to work.

On December 22, 1992, J. Howard met with Pierce, Hunter, Townsend, and Sorensen to review these matters related to Vickie, as well as other pieces of ongoing litigation. (Ex. 3245.) Sorensen's handwritten agenda included four specific "VLS Proposals": a "Family Farm Corporation," a "Modeling Corporation," a Grantor Retained Income Trust, or "GRIT," and adoption.[18] (Ex. 3245.) The agenda also

[17] The Court finds that the evidence before the Court sufficiently establishes the existence of a draft "catch-all" trust instrument prepared by Edwin Hunter. However, if the evidence had not been sufficient, the discovery abuses in this case might have led the Court to deem this fact as established as a sanction. *See* Fed.R.Civ.P. 37(b)(2)(A); Minute Order of October 5, 2001 Re: Evidentiary Sanctions.

[18] This was not J. Howard's plan to adopt Vickie's son, which came about later. Instead, at the time, J. Howard was

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included the pre-nuptial agreement as a separate agenda item. (Ex. 3245.) Unsatisfied with the results his attorneys had produced up until that time, J. Howard turned back to Sorensen.

J. Howard again told Sorensen that he wanted to marry Vickie. He told Sorensen that he wanted to provide Vickie with half of his "new community." (Ex. 62.) Sorensen testified that:

> new community was Mr. Marshall's words. He obviously intended to make her a gift. Well it's important to him because he wanted to share with her something he had done . . . "I am going to make this Koch Industries greatly enhanced in value and I want her to share in my achievements."

(Tr. of Tex. Probate Trial, Nov. 2, 2000, p. 181.)

Consistent with his propensity to avoid taxes, J. Howard did not want to trigger any gift tax liability, but wanted the gift to be "legally enforceable." (Id.) J. Howard defined for Sorensen what he meant by "new community," a term that he had previously employed when married to Betty. (Id.) As he had done with Betty, J. Howard defined "new community" as the growth of all his assets, even if they were separate property, during the time he was married to Vickie.

considering adopting Vickie, so as to avoid the generation skipping tax. Sorensen pointed out to him that Texas law might frown on the type of relationship he was having with his new "daughter."

In discussions with Sorensen, the two concluded that his principal asset was his interest in MPI, and therefore Koch Industries. (Ex. 62.) J. Howard believed that the growth in Koch Industries would come from its recent acquisition of the United Pipeline System, which he believed he had been instrumental in bringing about. (Id.) Although he did not plan to give her Koch stock outright, J. Howard was particularly interested in sharing with Vickie the fruits of that labor in the growth of the value of Koch stock.

J. Howard also made clear at that time that he wanted Vickie to have the benefit of the gift after he had passed away. J. Howard was aware that Vickie's career had a short life cycle. Although he could provide for her during his lifetime, he wanted her to have financial security and a comfortable retirement. J. Howard knew that Vickie had limited intelligence and experience. He would later call her "unteachable." Accordingly, he believed that some form of trust would be appropriate to provide for her after his death.

On his flight to Kansas the next day, Sorensen dictated a memo memorializing his conversation with J. Howard (the New Community Memo). (Ex. 62.) Sorensen and members of his firm researched the possibility of making such a gift to Vickie. Like all of J. Howard's lawyers, they ran into the dual problems of Koch stock valuation and Gift Tax liability. Indeed, because J. Howard was so much older than Vickie, a gift to her would also be subject to the Generation Skipping Tax of 55%. Sorensen eventually determined

that the gift could not take place at that time because of the tax liability.

J. Howard's tax concerns, however, were always a short-term problem. He planned to marry Vickie, and once he did there would be no tax liability for the Generation Skipping Tax or the Gift Tax. At one point, Hunter told J. Howard that he would solve all of his gift tax problems related to Vickie if he simply married her. Indeed, when J. Howard first told Hunter of his marriage to Vickie, he told Hunter that he had done so on Hunter's advice.

J. Howard's intent is also demonstrated by his interest in having children with Vickie. As noted *supra,* J. Howard seriously considered adopting Vickie's son Daniel. The adoption did not occur only because it became clear that Daniel's natural father would not give consent to the adoption. Moreover, Vickie and J. Howard attempted to have children of their own. J. Howard's intention to have children with Vickie demonstrates his interest in taking on substantially greater responsibilities toward Vickie and her children. These responsibilities would surely have included providing for his children's mother after he had passed away.

B. Vickie's Expectancy

J. Howard repeatedly proposed marriage to Vickie. On at least three specific occasions, J. Howard's proposals included specific promises of gifts to Vickie.

When the Tomball Ranch was purchased in 1992, Vickie was concerned about her right to the property because her name had been crossed out on the deed and she was wary of Pierce. Vickie explicity recalls that J. Howard told her "he wanted to take care of me and my son and give us security and he promised me half of everything that he had, that he wanted to always take care of me and always have me taken care of because of his age and all." (Dep. of Vickie, Dec. 28, 1999, p. 612-622.) Vickie's testimony before this Court was nearly identical on this issue.

Her second explicit recollection of donative intent was the purchase of a new 1993 Mercedes. Vickie wanted to get the title in her name and J. Howard stated, "honey, don't worry about it. Once we are married, you will have half of everything that I have."

The third time J. Howard made an explicit promise to her was when she returned to Houston in June 1994, after having been mobbed in Singapore on her Asian tour. "He just told me – I think he was missing me real bad because I was gone for a full week. And he just – I believe that he missed me really bad and he asked me to please marry him and that he loved me and that I would have half of everything that was his. I would have security for me and my son; and so finally I accepted his proposal." Shortly thereafter, Vickie and J. Howard were married.

No evidence was produced to show that anyone other than Vickie heard these specific proposals. However, the Court is guided by life experience in

making the rather unremarkable finding that most proposals are not trumpeted to the public or made in the presence of the family attorney, especially when the pursued object of matrimony has declined repeated proposals for nearly three years.

The privacy of J. Howard's proposals is corroborated by Harvey Sorensen. In March 1992, Sorensen had dinner with J. Howard at the River Oaks Country Club. At that dinner, Sorensen met Vickie for the first time. When she arrived, J. Howard asked Sorensen to excuse himself while J. Howard and Vickie spoke. While secretly watching the couple, Sorensen saw J. Howard give Vickie a ring and an envelope which Sorensen thought had money in it. J. Howard's promises are also corroborated by his pattern of sharing his "new community" with his second wife Betty and his seeking Sorensen's aid in creating a mechanism to give Vickie one-half of his "new community."

Although Vickie believed that J. Howard promised her one-half of his fortune, the Court finds that J. Howard always intended to give Vickie only half of his "new community." J. Howard, who used his wealth to impress women, did not explain to Vickie that what he meant by "half" referred to the "new community." Such a statement would be far less impressive.[19] Furthermore, such a statement would

[19] The dichotomy of the statements is illustrated by two hypothetical proposals:

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have meant little to Vickie, who was not familiar with what J. Howard meant by "new community," and would not be capable of grasping the distinction. Vickie therefore accepted J. Howard's promise at face value.

C. Edwin Hunter's Credibility

Edwin Hunter appeared before the Court to testify from December 12 to December 17, 2001. Hunter is a member of the bars of Louisiana, Texas, and Washington, D.C. He attended Louisiana State University for both undergraduate and law school. He began his legal career by working for a New Orleans firm in 1968. He later moved to Lake Charles where he became the head of the tax and estate planning division, and later the president, of a local firm. Since 1986, Hunter has been practicing in his own firm in Lake Charles, Louisiana, which is currently called Hunter, Blazer & O'Dowd (the Hunter Firm). Hunter represented MPI, J. Howard, and a number of the various trusts, all of which are now controlled by Pierce. Besides estate planning, Hunter's primary

> "Dear Vickie, please marry me and I will give you one-half of our 'new community,' which is a term I have coined and define as the appreciation of my assets, which primarily consist of Koch Industries stock, which is held by a holding corporation I created called MPI, the shares of stock of which are held in a living trust, which I amend from time to time;" or
>
> "Dear Vickie, please marry me and I will give you half of everything."

work for J. Howard in the years immediately preceding his death related to the on-going tax disputes between J. Howard and the IRS, which included questions on the value of gifts given to Lady Walker and the value of both MPI and Koch Industries.

Hunter was central to J. Howard's estate planning in the years prior to his death. Although Harvey Sorensen had taken over representation of J. Howard's estate planning in the early-1980's, and was responsible for drafting J. Howard's original living trust, Hunter began doing estate planning work for J. Howard in 1992. By mid-1993, Hunter had supplanted Harvey Sorensen as J. Howard's primary estate planning counsel. Hunter was responsible for the drafting of a number of J. Howard's final estate planning documents including the Amended and Restated Living Trust of July 13, 1994. The bankruptcy court found that Pierce "conspired with Hunter . . . " in tortiously interfering with J. Howard's gift to Vickie. *Marshall* I, 253 B.R. at 554. Obviously Hunter's credibility is therefore of utmost importance in determining the facts of the case.

For the reasons set forth below, the Court finds that Hunter lacks credibility as a witness. First and foremost, Hunter's lack of credibility was consistently demonstrated to the Court by numerous falsehoods made before the Court that were directly contradicted by documentary evidence in the case and, in some instances, by other witnesses on Pierce's side. Second, Hunter has several motives to distort the facts in this case: to cover up his wrongful conduct during the

events that give rise to this case; to preserve a settlement offer from the IRS on the value of MPI and Koch Industries in the continuing gift tax litigation, in which he continues to represent the Marshall family interests, now managed by Pierce; and to endear himself to Pierce, who has inherited J. Howard's wealth, whom Hunter admits was one of his largest clients. Finally, Hunter's lack of credibility was demonstrated by dishonest actions and his apparent willingness to abuse the high standing of his close family members.

Hunter's false statements are detailed first. The statements include, but are not limited to the following:

1. *Hunter's statement that he did not draft a "catch-all trust."*

During the proceedings before this Court, Hunter was asked where the draft of the "catch-all" trust was. Hunter claimed that he did not know. At that point in the proceedings, counsel for Vickie argued to the Court that it should sanction Pierce for his discovery abuses by designating as established that such a draft trust existed and would have been a mechanism to make gifts to Vickie. Hunter then stated that he "suddenly remembered" that the "catch-all" trust referred to a voting trust agreement for Compagnie Victoire. Hunter's "sudden" recollection, after six years of litigation in this matter is

incredible on its face. Moreover, such a recollection is contradicted by the facts of the case.

On December 15, 1992, Jeff Townsend sent Hunter a letter urging him to finish his work on four documents related to Vickie, all of which were to be presented to J. Howard at a meeting later that month. (Ex. 58.) Those documents were a draft-prenuptial agreement, a family farm corporation, a modeling corporation, and a "catch-all" trust. Hunter's billing records indicate that he and other members of the Hunter Firm worked on the first three documents prior to his meeting with J. Howard on December 22, 1992. (Ex. 649, p. 4.)

Not only do Hunter's billing records show his work on the first three items referenced in Townsend's December 15, 1994 letter, but they also demonstrate that he and members of the Hunter Firm worked on the "catch-all" trust. On November 10, 1992, his partner Glynn Blazier had a "[t]elephone conference with Finley Hilliard and Jeff Townsend regarding proposal to create trust for estate planning purposes." (Ex. 649, p. 2.) Additionally, Hunter's billing records show that he had a telephone conference with Blazier regarding the same. (Ex. 649, p. 2.). Hunter and Blazier again held a conference on a proposed trust on December 16, 1994. (Ex. 649, p. 3.) And finally, Hunter's billing records show that Glynn Blazier drafted a trust document on December 21, 1994. (Ex. 649, p. 4.)

That work on a "catch-all" trust was undertaken is also corroborated by Sorensen's handwritten agenda for the meeting with J. Howard, where he includes discussion of a GRIT, which was never produced. (Ex. 3245.)

Hunter claims that the term "catch-all" trust was used by Townsend because he was an oil and gas lawyer and thus did not understand the complexities of estate planning.[20] Townsend, however, as a corporate lawyer, would have been well aware of a voting trust and how it works, and would not mistakenly have referred to it as a "catch-all" trust.

Hunter further testified that the voting trust for Compagnie Victoire was necessary because Vickie was worried that she would not control the company because J. Howard owned all the stock. Thus, according to Hunter, a voting trust would assure her that she would control the company. Documents in evidence, however, show that Compagnie Victoire was not created until 1993 and that Vickie did not know of its existence until after its creation. Thus, Hunter could not have been preparing a document to ease Vickie's concerns about control of a corporation that she had no idea existed at the time. Moreover, the evidence shows that the voting trust for Compagnie Victoire was not put into place until several months

[20] Townsend did, however, carry out several personal, estate related, legal services for J. Howard, including investigating the possibility of adopting Vickie's son.

later. Furthermore, the Court is quite confident that, based upon her limited intelligence and understanding of business affairs, Vickie would not understand the workings of a voting trust. Hunter later claimed that the "catch-all" trust was subsumed into Compagnie Victoire.

Unfortunately, the Court must conclude that Hunter was untruthful. A draft "catch-all" trust was prepared, or, at the least, J. Howard directed Hunter to prepare one.

2. Hunter's statement that he did not know when the Fine Tuning Memo (Ex. 310a) was originally drafted.

In fact, Hunter knew full well that the Fine Tuning Memo was drafted on July 8, 1994. Hunter's billing records indicate that he drafted "Marshall post-matrimonial plan" on July 8, 1994. That corresponds with a statement in the Fine Tuning Memo that J. Howard had not told his children of his marriage to Vickie as of July 8, 1994. (Ex. 310a, p. 1.)

In the bankruptcy court, Hunter claimed that the "Marshall post-matrimonial plan" referred to in the billing records was the Amended and Restated Living Trust instrument dated July 13, 1994. (T2247.)[21] That

[21] As a result of this perjured testimony, there are portions of the bankruptcy court's proposed findings of fact and conclusions of law which mistakenly refer to the Amended and Restated Living Trust as the Fine Tuning Instrument. Pierce's

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was demonstrated to be false because Hunter's billing records indicate that Cherry Doucet drafted the Amended Living Trust on July 11, 1994, after receiving instructions from Hunter. (Ex. 649, p. 103).

This is important because it shows that the July 13, 1994 Amended and Restated Living Trust was changed to comport with the goals set forth in the Fine Tuning Memo which was drafted July 8, 1994, and therefore the Court can gain insight into the changes to the Living Trust by reference to the Fine Tuning Memo.

3. Hunter's statement that the reference "mischief" in the Fine Tuning Memo did not refer to gifts for Vickie.

Hunter's Fine Tuning Memo states that his plans would leave "less for mischief (and Miss Cleavage)." (Ex. 310a, p. 12.) Although Hunter admitted that "Miss Cleavage" referred to Vickie, he denied that "less for mischief" referred to allowing J. Howard to have less money that he could give to Vickie. Instead,

Amended Assignments of Error often quibble with the bankruptcy court's findings on the matter. (*See, e.g.*, Am. Assignments of Error ¶ 25: "There is no evidence that J. Howard ever saw or was informed of the contents of the Fine Tuning Document."; Am. Assignments of Error ¶ 27: "The Fine Tuning Document does not purport to change the provisions of the Living Trust. . . ."; *see also, e.g.*, Am. Assignments of Error ¶ 26, 28.) These contentions are the height of bad faith. *See* Fed.R.Civ.P. 11(b)(2), 11(b)(4).

Hunter disingenuously claimed that the phrase meant less for unspecified "waste." This deception was intended to hide what Hunter's perceptions about J. Howard were and his efforts to strip J. Howard of his assets.

4. Hunter's statement that he did not cause the Assignment, Promissory Note, and Pledge (Exs.287-289), to be backdated.

The Assignment, Promissory Note, and Pledge all purport to be dated June 1, 1994. However, Hunter's billing records show that Cherry Doucet of the Hunter Firm worked on "revisions of pledge" on July 11, 1994. (Ex. 649, 103, # 7535.) There is no record of a meeting with Pierce or J. Howard to sign these notes on June 1, 1994, nor are there records indicating that Hunter prepared these documents prior to June 1, 1994. Hunter's Fine Tuning Memo, which was drafted after J. Howard's June 27, 1994 marriage to Vickie, addresses these transactions and indicates that they should occur in the future. (Ex. 310a, p. 6, VII.A.4.)

In an attempt to explain away his billing records indicating that he had worked on these documents, Hunter furthered his dishonesty by suggesting that those records could refer to another pledge, but did not say what pledge that was, or show that it had ever been produced. Finally, Hunter suggests that maybe J. Howard and Pierce caused the documents to be backdated after they were delivered. However, the

dates on the documents are all typed, not hand-written in.

5. *Hunter's statement that he did not cause the donation of the GRAT to the J. Howard Marshall, II Living Trust to be backdated.*

The act of donation document purports to be dated January 13, 1994. Hunter testified that he did not backdate the document. That is contradicted by Hunter's Billing records which indicate that on July 12, 1994, Cherry Doucet of the Hunter Firm "[d]rafted donation of interest in GRAT." The January 1994 date is printed like the rest of the document.

6. *Hunter's Statement that Pierce was never shown the Fine Tuning Memorandum (Ex. 310a).*

Hunter's billing records for July 8, 1994 indicate that he drafted the Fine Tuning Memorandum and faxed it to Pierce. (Ex. 649, p. 102.# 7662.) ("Draft Marshall post-matrimonial plan; fax to E. Pierce Marshall. . . ."). This contradicts his statement of loyalty to J. Howard and demonstrates that he was working on Pierce's behalf.

7. Hunter's statement that he researched annulling J. Howard's marriage to Vickie to defend J. Howard from any actions taken by Pierce.

Hunter said that J. Howard told Hunter that he was very much in love with Vickie. Hunter, however, began researching annulment in the Fine Tuning Memo. Hunter testified that the reason he began researching annulment is that he was concerned that J. Howard would ask him if Pierce, holding J. Howard's power of attorney, could seek to have J. Howard's marriage annulled. This is completely inconsistent with Hunter's testimony that Pierce always followed his father's orders. Neither Hunter nor J. Howard would be concerned with Pierce seeking to annul J. Howard's marriage to Vickie if Pierce respected his father's decisions and never interfered with J. Howard's relationship with Vickie. Hunter was therefore either lying as to the degree of control exercised by J. Howard over Pierce, or, as the Court finds, as to whom Hunter was preparing the Fine Tuning Memo for.

8. Hunter's statement that he believed, in May 1995, that J. Howard would live for 5 years.

This is relevant because on May 26, 1995,[22] J. Howard allegedly approved two documents which

[22] This document may also have been backdated, *see infra*.

changed his estate plan. By the first document, the J. Howard Marshall, II GRAT, created in August 1993, sold back to MPI 47,288 shares of MPI. (Ex. 3376.) The other document was for sale of 63,051 MPI shares to MPI for a private annuity. (Ex. 3770.) Neither of these annuities were scheduled to make payments to J. Howard until March 1996. Hunter, like Pierce, testified that these annuities would have been economically beneficial to J. Howard had he lived for another five years. Hunter testified that he believed at the time that J. Howard would live for another five years. This is pure fiction.

In May 1995, J. Howard was already ninety years-old, and even reference to actuarial tables would suggest that he had less than five years to live. In fact, a year earlier, Hunter had done just that, finding that at 89, J. Howard had less than five years to live. (Ex. 310a, p. 7-8.) By May 1995, J. Howard had spent a large part of the previous five months in the hospital. On January 24, 1995, J. Howard had been rushed to the Hospital after his heart had stopped, and was only revived after CPR was administered. Townsend testified that he began looking into funeral arrangements for J. Howard in January 1995. Townsend testified that J. Howard never regained a healthy appearance in 1995, and he several times believed that J. Howard was close to death. If J. Howard's advanced age, his near-death experiences, the obvious breakdown of his physical health, his extended hospital stays, and his need for 24 hour nursing care did not make it clear enough to

Hunter that J. Howard would not live for another five years, in Spring 1995, J. Howard's physician, Dr. Reed, had diagnosed him with terminal, untreatable and inoperable stomach cancer. In April 1995, Dr. Reed opined that J. Howard might have as little as three months to live.

9. Other actions that demonstrated Hunter's lack of credibility

The Court's judgment of Hunter's credibility does not rest merely on these specific lies, made under oath before this Court (some of which were lies that he had [ ] previously made before the bankruptcy court). The Court also finds that his central role in the plan to drain J. Howard of his assets, which was undertaken in part to prevent J. Howard from making a substantial gift to Vickie, undermines his credibility.

This Court is not the first to question Hunter's character. Besides the bankruptcy court, which found that Hunter had conspired with Pierce to alter documents and deprive Vickie of her intended gift, Harvey Sorensen's firm, Foulston & Seifkin, found Hunter's ethics questionable. On June 20, 1994, Andrew Wright[23] prepared a research memo for Harvey Sorensen to advise him on his professional responsibilities relating to what Sorensen believed was Hunter's

[23] It appears that Andrew Wright is another attorney in Sorensen's firm.

"probable professional misconduct" in altering the GRAT, as discussed in Part IV.D.8.ii, *infra*. (Ex. 281, Memo p. 3.) According to Wright, Hunter had acted incompetently, disreputably, had refused to comply with tax regulations, and had done so with the intent to defraud. (Ex. 281, Memo pp. 5, 7.) Wright concluded that Hunter's conduct would be viewed by the Department of Treasury as "disreputable, intentionally fraudulent, and perhaps incompetent." (Ex. 281, Memo p. 7.) Wright recommended that Sorensen report Hunter to the relevant disciplinary bodies. (Id.)[24]

Finally, the Court is concerned that Hunter acted unethically in attempting to impress Pierce with his family's judicial prominence. Vickie's counsel argued that Hunter and Pierce were involved in planning to use these connections to gain an advantage in dealing with J. Howard's estate.

The Fine Tuning Memorandum prepared by Hunter includes statements that deal with estate planning once J. Howard had married Vickie. (Ex. 310a.) Up until Hunter drafted the Fine Tuning Memorandum on July 8, 1994, J. Howard had been co-trustee, along with Pierce, of the J. Howard Marshall, II Living Trust. On page 3 of that Memo,

[24] While the Court has no information as to Sorensen's eventual actions, Foulston & Siefkin informed Pierce and J. Howard that they would not second-chair the tax litigation behind Hunter. Although no reason was given to the Court, the Court believes that Sorensen and his firm did so in a successful effort to disassociate themselves from Hunter.

Hunter addresses concerns about how to choose a successor trustee upon J. Howard's death. On page 3, paragraph d, Hunter lists numerous options. The last of these is to "let longest serving federal judge in Texas appoint successor." (Ex. 649, p. 3.) This suggestion is out of place considering that state courts, not federal courts, are primarily responsible for probate matters. *See Marshall III,* 264 B.R. at 621. In the next sentence, Hunter's thinking becomes more clear: "[sidebar . . . my father is now the longest serving federal judge in the United States]" (Ex. 649, p. 3.) (Brackets in original.)

Hunter's father is the Honorable Edwin F. Hunter, Jr., Senior District Judge for the Western District of Louisiana, and as Hunter's Fine Tuning Memorandum indicates, he is the longest serving federal judge in Louisiana and the United States, having been appointed to the Bench by President Eisenhower in 1953.

When taken in context of the other events in this saga, Hunter's self-styled "sidebar" is not an innocuous note to himself. On the next line of the Fine Tuning Memorandum, Hunter's suggestion for the Living Trust was to "[p]ermit the trustee to re-situs trust if it gives an advantage." (Ex. 310a, p. 3.) Indeed, the Living Trust was later re-sited to Louisiana, where Pierce initiated succession proceedings. *See Howard Marshall Charitable Remainder Trust,* 709 So.2d at 662. Had Hunter's plans been followed through with, the longest serving federal judge in the state of the trusts' new situs, his father, would have

been given authority to choose a successor trustee. There is no evidence before the Court that these thoughts ever evolved past the planning stages, or that Judge Hunter was even aware of his son's plan. However, these events demonstrate Hunter's apparent willingness to exploit his father's high position.

Vickie's counsel points out, however, that this is not the only instance where Judge Hunter is referred to in connection with this matter. Vickie's counsel also argued that Hunter and Pierce were involved in attempting to solicit advice from a judicial officer. On January 27, 1995, Harry Winston sued J. Howard over a bounced check that he had written while purchasing jewelry for Vickie. Disputes arose between Vickie and Pierce, as J. Howard did not have the cash to cover the check. Pierce had been responsible for solving the problem and returning the jewelry to Winston. Vickie, however, never returned the jewelry, and Harry Winston sued. On April 22, 1996, Judge Audrey Collins of the Central District of California, issued findings of fact and conclusions of law in that matter, and entered judgment in favor of Harry Winston. This ruling upset Pierce. In response, Pierce sent a memorandum to Edwin Hunter, outlining numerous strategic alternatives for the Harry Winston case, as well as for Vickie's bankruptcy. (Ex. 431.)[25]

[25] During the presentation of the case to the Court, several documents were made available to Vickie's counsel by Pierce, with Pierce reserving the right to object to them based on

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Part 2.B of that memorandum details how Pierce and his lawyers could determine his options for legal recourse. Included is the following passage:

> 2. Obtain all the pleadings and briefs for review by Judge Hunter. I very much appreciate this very valuable step. It would be most helpful to have the Judge's advice regarding what elements are needed to:
>
> A. Successfully move for a new trial and prevailing;
>
> B. Successfully move for an appeal and prevailing.
>
> 3. After the Judge has had a chance to review the case, Jeff [Townsend] needs to visit with him to discuss the issues and the Judge's advice . . . .

privilege. The Court has not relied on any document as evidence that is subject to a legitimate claim of attorney-client privilege. However, Exhibit 431 is potentially privileged communication from Pierce to his attorney Hunter. The Court, however, finds the exhibit admissible for two reasons. First, throughout the proceedings, Pierce has contended vehemently that Hunter did not represent him, and Hunter has testified to the same effect. Second, this document is admissible under the crime-fraud exception to the attorney-client privilege. *See, e.g.*, *United States v. Chen*, 99 F.3d 1495, 1503 (9th Cir.1996). Here, the communication shows Pierce arranging to have Townsend seek information from a federal judge about a separate pending civil action. This constitutes a fraud on the court and potentially obstruction of justice in violation of 18 U.S.C. § 1503. Pierce's objection of privilege is therefore overruled.

> 4. Seek the advice of other "wise men" who may be able to help us achieve our objectives A & B above.

(Ex. 431, pp. 1-2.) Pierce confirmed during his testimony that "Judge Hunter" referred to Edwin Hunter's father, Judge Edwin F. Hunter, Jr. Later in the memorandum, where he writes:

> I think we were badly home-towned, but perhaps it is good because we will be more ready next time for what to expect from the California courts. We need to modify our behavior and analysis accordingly. That is the purpose of the experience. We need to use aggressively every opportunity to home-town them in Louisiana,

(Ex. 431, p. 4.)

This memorandum makes clear that, at the very least, Edwin Hunter had offered to Pierce the services of his father, a sitting federal district judge, in analyzing and recommending litigation strategy for a client in an attempt to overturn the ruling of a fellow district court judge.[26] In addition, the phrase "other wise men" appears to refer to other judicial officers in the state.

This conduct gives rise to even more serious questions about Hunter's character. If Hunter was

[26] The fact that the memorandum was written by Pierce indicates that Pierce was complicit in this conduct.

merely seeking advice, on behalf of Pierce, about the prospects for winning a new trial or an appeal, he could have approached dozens of well respected appellate law firms.[27] Approaching a judge, in violation of the principles of ethics, suggests that Hunter was seeking to use Judge Hunter's influence, not just his legal skills, in order to further Pierce's litigation posture. Such an approach is unquestionably unethical, potentially criminal, and certainly shows Hunter's character to be untrustworthy.

The Court concludes that Edwin Hunter's testimony consisted of numerous lies, and that he has no credibility as a witness.[28]

D. Tortious Acts by Pierce and Hunter that Deprived Vickie of her Expectancy

1. Pierce's Knowledge and Motivation

From early in J. Howard's relationship with Vickie, Pierce knew of the gifts that J. Howard was giving to Vickie. He was aware of J. Howard's pattern of giving to his lovers based on his involvement with the Lady Walker litigation and the related gift tax

[27] The Court notes that Pierce has been represented in this matter by the Los Angeles firm Jeffer, Mangels, Butler & Mamaro, one of the most prominent firms in the city.

[28] In light of Hunter's behavior, the Court encourages the United States Attorney for the Central District of California to undertake a close review of the record in this case to determine whether to seek an indictment for perjury under 18 U.S.C. § 1621.

litigation. Pierce knew that J. Howard was starting that same gift-giving pattern with Vickie. He knew that J. Howard had purchased the Tomball Ranch for Vickie as he had signed the deed as co-trustee of the Living Trust.

In the late fall of 1992, J. Howard was preparing to marry Vickie and planning on making a substantial gift to her. Pierce was present at meetings between his father, Hunter, Townsend and Sorensen when J. Howard detailed the type of gift that he was going to make. J. Howard had asked Pierce to coordinate all the details, and accordingly Pierce had frequent contact with J. Howard's lawyers and knew what their assignments were.

J. Howard's plan to give Vickie money based on the value of Koch Industries stock was immediately problematic. Pierce had been responsible for managing litigation with the IRS, one of the central components of which was the value of Koch Industries stock. Pierce and Hunter recognized that if Vickie had any interest in MPI stock, as proposed in the New Community Memo, she would have an interest in increasing the value of that stock. The teaming of a widowed wife with the IRS loomed as a bad combination in the goal of keeping down the value of Koch stock. This was crucial to Pierce, who stood to inherit MPI, and owned Koch stock in his own right. Pierce would therefore tolerate his father's extravagant gifts to Vickie in the form of houses, cars, jewelry and cash. But he could literally not afford to

allow J. Howard to give Vickie any interest in Koch or MPI.

2. The Replacement of Harvey Sorensen with Edwin Hunter

In Edwin Hunter, Pierce found a person who would aggressively pursue his interests. Hunter had an obviously low opinion of Vickie. He was far more willing to be aggressive in tax litigation than Sorensen. Hunter knew that Pierce was already managing the details that J. Howard so despised dealing with. Hunter's practice of law was all about details. He designed creative and intricate estate planning schemes on a daily basis, the success of which were based on the details of the plans. So while J. Howard would pass over details with a dismissive wave of his hand, Hunter knew that the devil, and therefore the power, was in the details. Hunter also knew that, in time, Pierce would control the interests of the Marshall family and MPI, whose representation could prove extremely lucrative to him.

Hunter was aware of J. Howard's long-held estate planning goals. J. Howard never wavered in his desire to leave Pierce in control of MPI and with his Koch Industries stock. But J. Howard's reckless cavorting with Vickie could endanger those plans. Hunter therefore would act as a guardian of J. Howard's interests.

Sorensen was not so amenable. His ethics were different than Hunter's. Pierce eventually informed Sorensen that he was no longer responsible for

Marshall family work. (Ex. 230.) This decision was J. Howard's, who preferred Hunter's more aggressive approach to the IRS. However, this decision was made at the counsel of Pierce, who was given the ultimate responsibility for terminating Sorensen.

J. Howard was notoriously loyal to the people that had worked for him. In the 1960's, when Finley Hilliard had left the accounting firm of Peat Marwick, J. Howard had demanded that his business go with Hilliard, and threatened Peat Marwick that he would personally defend Hilliard if they sued him. This loyalty would not allow him to terminate his attorney of ten years, a man that had become his closest legal adviser and a friend that stayed at his home in Houston, without some outside provocation.

Pierce was responsible for following the details of the Lady Walker litigation. He was the only person that could describe the advantages of one or the other to his father. J. Howard also placed immense trust in Pierce. Thus, when Pierce suggested to J. Howard that Hunter replace Sorensen, J. Howard consented.

3. August 1993 Changes to J. Howard's Estate Plan

Evidence of the scheme to drain J. Howard of his assets is demonstrated by the immediate changes to J. Howard's estate planning once Hunter took over. In December 1992, Sorensen had devised a method for J. Howard to begin to give up his controlling interest in MPI. (Ex. 60.) This was important for estate planning

reasons. By converting his voting stock to non-voting stock, it would be given a non-voting discount in valuation. Additionally, if he was able to bring his percentage ownership under 50%, he would not suffer the upward adjustment for a controlling interest and would be able to take a discount for a minority position. J. Howard, however, had never voluntarily given up control of anything in his life. He had insisted on being in charge. In his deposition in the Lady Walker litigation, he insisted that MPI never took directions from anyone other than himself. Accordingly, Sorensen had devised a plan for J. Howard to obtain an irrevocable proxy over Pierce's MPI stock. (Ex. 60.) J. Howard would then be able to control MPI by voting Pierce's stock.

In August 1993, Hunter told J. Howard that this arrangement was unworkable. He contended that if J. Howard gave stock to Pierce with an irrevocable proxy, it would be an incomplete gift, and subject to the estate tax upon J. Howard's death. Despite his proven creativity in tax and estate matters, Hunter told J. Howard that the only way to give up his controlling interest was to sell his shares and trust Pierce to vote the way J. Howard told him to.[29]

[29] The Court suspects that there were several other ways of insuring J. Howard's control of MPI, including an irrevocable proxy on the shares owned by Eleanor Pierce Marshall Stevens, who appeared to leave many business decisions in her ex-husband's hands, or by giving J. Howard a proxy of the shares of MPI that Pierce had previously acquired, which, combined with

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In preparation for his meeting with J. Howard, Hunter sent him an estate planning packet of 151 pages. (Ex. 3285.) Based on his past experience with J. Howard, including his drafting a pre-nuptial agreement for J. Howard and Vickie in December 1992, Hunter knew that J. Howard wanted legal documents that were a page or two long. Instead of following these well-known preferences, Hunter buried J. Howard in paperwork, filled with details, that Hunter knew J. Howard would never review.

J. Howard was also capable of being controlled by Hunter and Pierce because of his physical inability to read as a result of having developed cataracts. Thus, J. Howard only read papers printed in extremely large type, and then only with the assistance of reading glasses. J. Howard's practice was to have someone read the document to him. Hunter was responsible for reading a number of documents to J. Howard.

On August 25, 1993, J. Howard signed several documents relating to MPI and his estate planning:

i. J. Howard resigned as a trustee of the MPI voting trust, the trust that technically controlled the voting stock of MPI. (Ex. 3289.)

ii. He sold to Pierce 35,466 shares of MPI stock, representing 15% of the outstanding stock of MPI.

J. Howard's 49% interest, would be sufficient to keep J. Howard voting a majority of the MPI shares, and thus in complete control.

(Ex. 3292.)[30] Pierce bought those shares with a promissory note in the sum of $17,355,000, at a rate of 6.26% interest. (Ex. 3291.) The note called for Pierce to pay $575,000 on the first of January and July of each year, with a balloon payment in ten years (the Pierce Note). (Id.)[31]

iii. J. Howard signed a Grantor Retained Annuity Trust (GRAT). (Ex. 3293.) J. Howard transferred 47,288 shares of MPI, representing 20% of the outstanding shares, to the GRAT. J. Howard would receive a payment from the GRAT each year for five years, after which the shares would transfer to Pierce.[32]

iv. J. Howard gave Pierce an outright gift of 2044 shares of MPI, with Pierce responsible for paying the gift taxes. (Ex. 3288.)

v. J. Howard sold back to MPI 14,065 shares in order to cancel his outstanding debt to MPI. (Ex. 3294.)

[30] At the time, J. Howard owned 164,252 shares of MPI stock. The total number of outstanding MPI shares at the time was 236,440. J. Howard therefore owned approximately 69.5% of MPI before these transactions.

[31] J. Howard did not live ten years to receive the balloon payment. The Pierce Note, meanwhile was later assigned to the Living Trust, of which Pierce was the primary beneficiary. The result was that Pierce avoided paying a substantial sum due on the note.

[32] In the event of death, most of the shares in the GRAT would revert to J. Howard's estate.

The result of these transactions was that J. Howard's ownership interest in MPI was reduced to 65,389 shares, a mere 29% of his corporation. The beneficiary of these transactions was Pierce. Although now legally in control of MPI, Pierce's goal was to prevent a transfer to Vickie that might increase the purported value of his shares and undermine the ongoing litigation with the IRS.

4. The Wedding of J. Howard and Vickie and the Surveillance of J. Howard

On June 27, 1994, J. Howard married Vickie. Several members of J. Howard's personal and MPI staff were invited, although Pierce was not. The next day, Pierce and Hunter held a conference call with Henry Schlesinger, who was invited to the wedding. (Ex. 649, p. 101). Pierce and Hunter likely found out about the wedding that day from Schlesinger.[33] This

[33] Hunter claims to have found out in Houston from J. Howard himself. There are no records of this meeting with J. Howard. As noted *supra*, the Court does not find Edwin Hunter credible. Nevertheless, it is clear that Hunter knew about the marriage before July 6, 1994, when J. Howard left to visit Vickie in Los Angeles. Pierce claims that he found out about J. Howard's wedding on July 11, 1994 from Dan Hedges, another of J. Howard's attorneys. The Court finds this incredible. The evidence in Hunter's billing records indicates that Hunter faxed to Pierce the Fine Tuning Memo, which refers to the wedding (Ex. 310a), on July 8, 1994. (Ex. 649, p. 102.) Additionally, Hunter's billing records show numerous conversations with Pierce after Hunter had found out about J. Howard's wedding, and there is every reason to believe that Hunter told Pierce. Finally, J.

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began a flurry of activity by Pierce, Hunter and others to alter J. Howard's estate plan so as to prevent Vickie from receiving a gift and undermining their hard work to reduce the apparent value of MPI stock.

On July 6, 1994, J. Howard left for Los Angeles to visit Vickie. (Ex. 3326, p. 4.) With Pierce's authorization, Dan Hedges hired private investigators to trail J. Howard in California. Pierce had the bills sent directly to his home address in Dallas. Pierce claims that this trail was for J. Howard's protection because Vickie's bodyguard, Pierre DeJean posed a safety risk to J. Howard. The Court, however, finds that the surveillance was not for J. Howard's protection, but instead was to guarantee against J. Howard signing a new will while in California. The Court's finding is based on the following reasons.

i. Pierce and Hedges did not tell J. Howard's driver Arnold Wyche, or J. Howard, that J. Howard was being trailed for his own safety. If Pierce was concerned with J. Howard's safety, he would have told J. Howard and Wyche to warn them of the potential threat.

Howard's wedding was common knowledge at the MPI offices, and Pierce had by that time become President of MPI. It is therefore incredible that Pierce did not know about the wedding shortly after it occurred. Evidence of surveillance placed on J. Howard while he traveled to Los Angeles after the wedding further corroborates this finding.

ii. The surveillance in California ended between 7 PM and 9 PM in the evening. (Ex. 3326.) If DeJean posed a serious threat to J. Howard's safety, it would have been a twenty-four hour threat. Instead, the surveillance ended around the time that J. Howard typically went to bed and would therefore not be able to sign a new will or other document in favor of Vickie.

iii. The surveillance was of J. Howard, not Pierre DeJean. (Ex. 3326.) If Pierce were concerned about J. Howard's safety, he would have DeJean trailed to check his contacts and his actions.

iv. On February 17, 1995, Townsend sent a letter to Vickie's lawyer Patrick Freydl. (Ex. 84.) He indicated to Freydl that:

> [i]t has been reported by reliable sources that either a will, or other type of contract, was executed by Mr. Marshall in California, and that you prepared such a will or contract. On behalf of Mr. Marshall, demand is made for immediate production of any document executed by him .... In order that there is no question as to my exact request, please note that I am requesting the original ....

(Ex. 84.)[34]

[34] Townsend's request for the original is particularly troubling. Given the record of document tampering in this case,

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On February 24, 1995, Dan Hedges sent a letter to Pierce, copied to Hunter and Townsend, informing Pierce that Freydl had denied writing a will. (Ex. 675.) The letter states that this contradicts DeJean's information on a will. Pierre DeJean was evidently the "reliable source" that Townsend referred to. It is unlikely that Pierce considered DeJean a danger to J. Howard in July, but by February considered him a "reliable source."

v. The investigators hired by Pierce kept a liaison with the Federal Bureau of Investigations based on their stated fear that Vickie and DeJean might become involved in interstate or wiretap fraud in their attempt to obtain J. Howard's assets, but never contacted local authorities to express their professed concerns about J. Howard's physical safety. (Ex. 3326, p. 12).

vi. In the Fine Tuning Memo of July 8, 1994, Hunter indicated the major concerns regarding J. Howard traveling to California:

> J. Howard's office believes Vickie's attorneys in California may be preparing documents for his signature, possibilities include:
>
> a. A new will
>
> b. Adoption of Vickie's child

there is an obvious concern that an original in the hands of Pierce and Hunter would be altered or destroyed.

c. Gifts to Vickie

(Ex. 310a, p. 1.)

The concerns of Pierce, Hunter, and "J. Howard's office"[35] demonstrate that they believed that J. Howard could in fact be controlled and tricked into signing away his estate. Their concern was not unfounded. Pierce and Hunter had already drained him of significant assets in August 1993. They now set out on a plan to continue that drain before Vickie's lawyers could get their hands on J. Howard's assets. Despite all the concern of Pierce, Hunter, and "J. Howard's office," there was never any evidence introduced that Vickie or her lawyers attempted to have J. Howard sign a will, adoption documents, any gift instrument, or any other document divesting J. Howard of his wealth.

5. July 1994 Changes to J. Howard's Estate Plan

On July 8, 1994, Edwin Hunter drafted the Fine Tuning Memo. (Ex. 310a.) This is reflected in his billing records for July 8, 1994. (Ex. 649, p. 102, # 7662.) This memo formed the foundation of plans to prevent J. Howard from making a gift involving MPI or Koch stock that would disrupt the gift tax litigation or run the risk of valuing Koch stock at a high

[35] This likely refers to Eyvonne Scurlock and Henry Schlesinger.

price. The thrust of the plan was to make sure that any property owned by J. Howard be put into his living trust and to make his living trust irrevocable so that J. Howard would be unable to make any gifts to Vickie. Hunter's Fine Tuning Memo indicates the importance of making the living trust irrevocable. Were J. Howard, then eighty-nine years old, to be declared incompetent, Vickie, as J. Howard's wife, would have the preference under both Texas and California law of being appointed guardian of J. Howard. (Ex. 310a, p. 2, B.1-2.) Hunter notes that "[h]er appearance as J. Howard's guardian might disrupt the estate plan and could lead to litigation with the family." (Ex. 310a, p. 2, B.4.) Hunter and Pierce were concerned that Vickie's meddling might lead to a transfer of property away from Pierce and to her, leading to a high valuation of Koch stock. Moreover, making the trust irrevocable would leave "less for mischief (or Miss Cleavage)," meaning Vickie. (Ex. 310a, p. 12, 2.a(2).) Hunter's office immediately began drafting several documents to accomplish this goal.

Along with several other goals, Hunter and Pierce addressed the August 25, 1993 Pierce Note. Under Texas Community Property law, income derived from J. Howard's separate property would be community property. (Ex. 310a, p. 4, IV.A.1.b.) Hunter's office then prepared documents to prevent Vickie from ever being able to collect any of the money from Pierce's payments on the note. J. Howard

signed a promissory note to MPI for $5,618,074. (Ex. 288.)[36] To secure this debt, J. Howard pledged to MPI the August 25, 1993 Pierce Note. (Ex. 289.) This would allow MPI, now run by Pierce, to intercept the note payments before they reached J. Howard and Vickie, and use the payments to pay down the debt owed to MPI. (Ex. 310a, p. 6, VII.A.4.b.) Because the Living Trust was also being made irrevocable, Vickie would never be able to recover those proceeds. Hunter was concerned that by encumbering the note, there might be an improper interference with Vickie's community property interest in the income stream. To solve this problem, those documents were then backdated to June 1, 1994, before J. Howard and Vickie were married, as detailed in Part IV.D.8.iv, *infra*. By backdating the note, it also served to void any instrument assigning the note to Vickie as a gift that they feared J. Howard might have signed while in California.

On July 12, 1994, Hunter, Pierce, Jeff Townsend, Hilliard, Scurlock, and J. Howard met at the MPI offices in Houston. Pierce at that time confronted his father about his marriage, at which point J. Howard

[36] The comments in Hunter's Fine Tuning Memo suggest that this was money that J. Howard already owed to MPI. (Ex. 310a, p. 6, VII.A.) Indeed, it was J. Howard's custom to support himself by borrowing funds from MPI, which in turn borrowed funds from Texas Commerce Bank, backed by MPI's interest in Koch. J. Howard would then settle the debt with MPI by selling shares of stock back to MPI. These debts, however were unsecured.

admitted to Pierce the he had married Vickie. The group briefly discussed estate planning options with J. Howard and was ordered to reconvene the next day.

On July 13, 1994, and again on July 15, 1994, Hunter, Pierce, Townsend, Hilliard, Scurlock, and J. Howard met at the MPI offices in Houston to sign J. Howard's estate planning documents. Because J. Howard could not see well enough to read the document, Hunter read to J. Howard what he considered to be the pertinent provisions of the Amended and Restated Living Trust. Pierce was in the next room when Hunter read the document to J. Howard, but was present when J. Howard allegedly signed the Amended and Restated Living Trust. During this period, J. Howard also signed the Assignment, Pledge, and Promissory Note that purport to be dated June 1, 1994. (Exs.287-289.) J. Howard also signed an act of procuration (power of attorney) and a donation of his membership in the River Oaks Country Club to the Living Trust during this period.

After J. Howard had signed the Amended and Restated Living Trust, a new page two of the trust was inserted, as detailed in Part IV.D.8.v, *infra*. The new page contained the provision stating that the trust was irrevocable. Because J. Howard was totally dependent on Hunter to inform him of the contents of the document, he was unaware that the amendments made the trust irrevocable. The evidence shows that nearly a year later, he still believed that he had total control of his assets. On May 26, 1995, J. Howard

made a tape recorded statement to the judge in the guardianship proceedings wherein he stated: "despite what Pierce or anybody says, I have been a successful businessman and am not broke." (Ex. 364.) By that time, however, J. Howard had been stripped of his remaining assets and was technically broke. Furthermore, Glenn Johnson, who was appointed by the Texas probate court as J. Howard's temporary guardian on May 31, 1995, testified in the Texas probate proceedings that he had a conversation with J. Howard about his estate plan. According to Johnson, J. Howard's opinion of the changes to his estate plan were as follows: "He trusted Pierce and had no problem with it, and if he ever didn't like it, he could change it." (Ex. 3638.) However, because the Living Trust had been made irrevocable, and J. Howard divested of all his MPI stock, he could not change his estate plan. J. Howard had been duped.

Following the signing of the Amended and Restated Living Trust, the document was given to J. Howard's assistant Scurlock, who also notarized the signatures. Four to six days later,[37] on July 19, 1994,

[37] There was a disagreement about whether the Amended and Restated Living Trust was signed on July 13, 1994 or July 15, 1994, thus it is unclear whether there were four or six days between its execution and its delivery to Townsend for recording. This is due in part because page one and page twenty-two indicate two different dates of execution. Although this is an example of the many questionable factors of the document, *see* Part IV.D.8.v, *supra*, the discrepancies between July 13 and July 15 appear to be immaterial.

Scurlock gave the document to Townsend for him to record. Townsend then took the document from Houston to his office in Lake Charles, Louisiana. The next day, Townsend had a stack of copies of the document made at his office. In his office, Townsend had a relatively modern photocopy machine equipped with a document collator. Townsend's plan was to record the document and provide the copies to the county recorder to certify, saving the time and expense of having the county recorder copy the documents.

The morning after Townsend had the copies made, he flew from Lake Charles to Midland, Texas. From Midland, Townsend drove approximately 30 miles south where he recorded the Amended and Restated Living Trust in Glasscock County, Texas. Glasscock County is one of the smallest counties in Texas. It has a single courthouse, but there are no lawyers in the County. Glasscock County's sole prior claim to fame was that it had a lakebed that filled every 20 years.

Upon arriving at the Glasscock County Courthouse, Townsend met the county clerk, Betty Pate, and her deputy, Shirley Wood. They informed Townsend that they could not use his copies, and would instead have to make the copies of the document in the county offices. Townsend discarded the copies he had brought from Lake Charles and Pate and Wood proceeded to make approximately 40 copies of the document on the Glasscock County copy machine, and collated the copies by hand. The original was

then recorded and the copies certified. Townsend then used the certified copies to record the trust instrument by mail in several counties in Texas and parishes in Louisiana.

Had the Living Trust been recorded in Harris County, the public records would have been more readily accessible, and it is possible that the press would have found out the details of J. Howard's personal finances. Indeed, another of J. Howard's lawyers, Dan Hedges, had obtained public record information of J. Howard's wedding to Vickie. Recording the document in the smallest county in Texas made that nearly impossible. One explanation for this is that Pierce did not want a story printed, or a friend of J. Howard's telling him, about the Living Trust being made irrevocable.

6. *Further Changes to Estate Plan Between July 1994 and May 1995*

Over the next year, J. Howard's health deteriorated. He was hospitalized on three different occasions, diagnosed with terminal cancer, and never recovered his physical strength. J. Howard's ill-health engendered a guardianship dispute between Pierce and Vickie. On May 31, 1995, the Texas probate court appointed Glenn Johnson the temporary guardian of the person of J. Howard. After Johnson's report to the probate court, Betty Morgan was appointed permanent guardian.

Several final changes to J. Howard's estate plan were undertaken during this time. Pierce and Finley Hilliard, as trustees of the J. Howard Living Trust, re-sited the trust to Louisiana. (Ex. 341.) As Hunter had written in the Fine Tuning Memo, this was an option to exercise if it would give them an advantage. (Ex. 310a.) By moving the trust from Texas to Louisiana, Pierce, Hunter and Hilliard were taking advantage of Hunter's familiarity with Louisiana – they were preparing to "hometown" any opponents, as Pierce would later describe it. (Ex. 431.)

Acting under his power of attorney, Pierce signed a document renouncing J. Howard's right to collect distributions from the living trust. (Ex. 145.) The renunciation was purportedly signed on December 28, 1994. According to Pierce, he read the document over the phone to J. Howard, who was then at his home in Houston. Pierce claims that J. Howard then told him to sign the document. This claim is not credible. It was J. Howard's intent to keep for himself as much income as he could, allowing him to finance his lifestyle and his gifts to Vickie. He had no interest in renouncing his right to obtain income from the living trust.

Pierce may have signed this document in the Spring of 1995, while he was feuding with Vickie over spousal support and guardianship. Pierce had discontinued paying Vickie's bills, and by renouncing J. Howard's right to demand income from the Living Trust, he would be cutting off Vickie's derivative rights.

Furthermore, the document is irregular on its face. It was notarized by Eyvonne Scurlock. As detailed in these findings, Eyvonne Scurlock fraudulently notarized several backdated documents prepared by Hunter. Her notary book bears no record of having notarized the Renunciation on December 28, 1994. (Ex. 676.) Moreover, Finley Hilliard's signature as a co-trustee of the living trust was not notarized until February 22, 1996, more than six months after J. Howard's death. (Ex. 145.)

Accordingly, the Court finds that the document was not signed in December 1994.

7. May 1995 Changes to the Estate Plan

The last set of changes to J. Howard's estate planning purportedly took place on May 26, 1995. J. Howard's remaining 63,051 shares of MPI stock were sold back to MPI in exchange for a private annuity. (Ex. 3370.) Under the terms of the annuity, MPI would pay J. Howard $7,906,006 on March 31 of each year, commencing in 1996, as long as J. Howard was alive. (Ex. 3370.)[38] J. Howard did not live to see March 31, 1996, and accordingly the MPI ended up paying nothing for J. Howard's remaining shares. Nor could J. Howard be reasonably expected to live until March 31, 1996. J. Howard had been diagnosed with terminal stomach cancer in Spring 1995. Pierce, who

[38] The annuity provided that the payment would increase by 20% each year.

signed the Sale for Private Annuity as both the co-trustee of the J. Howard Living Trust and as President of MPI was entirely aware of J. Howard's condition. He had been advised of the diagnosis by J. Howard's physician Dr. Reed in April 1995. Pierce therefore arranged to strip J. Howard of his final vestiges of ownership in MPI for no consideration.

Also purportedly on May 26, 1995, the GRAT sold to MPI the 47,288 shares of MPI that it held in exchange for a $24,753,376 note. (Ex. 3376.) The terms of the note were that MPI would pay interest of approximately $1,898,584 to the GRAT each year, with the principle on the note due in 2010.[39] (Ex. 90.)

[39] Pierce testified that, had J. Howard lived until March 31, 1996, MPI would have had to borrow nearly $10 million to finance the payments due on the private annuity and note. At the time, MPI had obtained a $15 million line of credit from Texas Commerce Bank, secured by MPI's interest in Koch stock. According to Pierce, Texas Commerce Bank had become concerned with the amount of money outstanding to MPI. It had insisted that MPI reduce its debt to $12 million and that it stop taking out loans to finance J. Howard's personal spending. It is therefore unfathomable how Pierce would have been able to convince Texas Commerce Bank to nearly double MPI's line of credit to pay the amounts due under the note and the private annuity. Moreover, even if it had been able to borrow enough to pay the amounts due in 1996, Hunter testified that the private annuity would only be a good business decision for J. Howard if he lived for five years or more. Thus, MPI would have had to borrow nearly $50 million over five years to finance J. Howard's personal spending, at a time when its lender had reduced its line of credit from $15 million to $12 million. The testimony that the May 1995 transactions were legitimate and sound business

(Continued on following page)

Transferring the stock out of the GRAT was necessary to prevent MPI stock from falling into Vickie's hands, because if J. Howard were to die before 1998, 99% of the corpus of the GRAT would return to J. Howard's "estate." (Ex. 3293.) Pierce had been continually concerned that J. Howard might have signed a will in California, giving money and possibly leaving his residuary estate to Vickie. This concern motivated him to conduct surveillance on J. Howard while he was in California, (Ex. 3326), was expressed in Hunter's Fine Tuning Memo, (Ex. 310a, p. 4, "C. Effect of a Clandestine California Will"), was evidenced by Townsend's letter to Pat Freydl indicating that Townsend had information that Freydl had prepared a will for J. Howard, (Ex. 84), and was the motivation for making the Living Trust irrevocable.

Pierce and Hunter both testified that these changes were undertaken at J. Howard's direction. This was in the face of the obvious incredibility of a ninety year-old man, diagnosed with terminal cancer, agreeing to give up his last assets in exchange for an annuity that he would never live to see paid. Moreover, Pierce did not believe that J. Howard had the capacity to make these decisions. On May 26, 1995, Pierce signed a Directors Consent stating that J. Howard no longer had the capacity to act as a director for MPI, and removed him from the MPI board. This made Pierce the sole director. (Ex. 3375.)

decisions, undertaken at the behest of J. Howard, is contradictory and therefore not credible.

Even if the Court were to view Pierce's actions as good faith efforts to preserve his father's long-held estate planning wishes, which it does not, his actions still defy both the law and fundamental ethics. Beyond the legal questions that the Court has had to deal with, there are philosophical questions as to whether an elderly person has the right to spend his money as he chooses, even if he does so in a foolhardy way. Whatever his personal actions, J. Howard had earned his life's fortune, and Pierce never had the right to interfere with the way that J. Howard saw fit to spend it.

8. Destroyed, Altered, Backdated, and Fraudulent Documents

Pierce and Hunter's actions of slowly draining J. Howard of assets in order to prevent a gift to Vickie were egregious in nature. What is worse, however, is that many of the documents at issue in the case were destroyed, backdated, altered, or prepared and presented to J. Howard under false pretenses. This was done in order to prevent Vickie from receiving funds, out of fear that J. Howard might sign a will or other gift instrument at Vickie's behest, and to avoid the legal consequence of important dates in J. Howard's final years including his marriage to Vickie and the appointment of a guardian ad litem to manage his affairs.

The backdating and altering of the documents was done with the full knowledge of Pierce. Most of

the backdated documents were prepared by Edwin Hunter, whose brilliant machinations on estate planning Pierce relied on to devise the necessary actions. Finally, many of the backdated documents were notarized by Scurlock who violated her oath by signing false notarial statements.

The documents subject to destruction, backdating, altering or false pretenses were:

i. The draft of the catch-all trust prepared by Hunter prior to his December 1992 meeting with J. Howard

As detailed in Part IV.C.1, *supra,* the evidence shows that Hunter prepared a "catch-all" trust prior to his December 1992 meeting with J. Howard, that was a mechanism for J. Howard to give a substantial gift to Vickie. That document was never produced by Hunter.

ii. The Grantor Retained Annuity Trust (GRAT) (Ex. 3293)

This document was originally signed by J. Howard on August 25, 1993, and held 47,288 shares of MPI. The document was altered by Hunter in March 1994.

In early 1994, Harvey Sorensen, who was responsible for filing tax returns for MPI, pointed out to Hunter that the copy of the GRAT that he had received in September 1993 was not qualified to hold

shares of a subchapter "S" corporation under the Internal Revenue Code, and therefore MPI's subchapter "S" election was in jeopardy. Although Hunter responded that it complied with an IRS Private Letter Ruling (*see* Ex. 133), he simultaneously directed Cherry Doucet to revise the GRAT. Doucet prepared revisions of the GRAT on March 2, 1994. (Ex. 649, p. 11.) Page two of the GRAT was then substituted. (Ex. 281, Sorensen letter stating his conclusion that the GRAT had been altered.) The revised GRAT added the following sentence to paragraph four of the GRAT: "Grantor may substitute property of equivalent value for the original trust corpus." (*Compare* Ex. 245 with Ex. 3293.) Because the substituted sentence added a line to page two, another line had to be deleted from the page so as to not disturb other pages, including the signature page. Paragraph 10(a) of the GRAT defined the Trustee's powers "[t]o sell at public or private sale . . . real estate. . . ." (Ex. 245.) The superfluous words "at public or private sale" were deleted, eliminating a line from paragraph 10(b), allowing the revised page two to be inserted in place of the original. (*Compare* Ex. 245 with Ex. 3293.)

Hunter then sent the revised pages to Sorensen. (Ex. 281.) Sorensen believed at first that the page was substituted and refused to sign the tax return until he had gotten an explanation from J. Howard or Hunter. Sorensen later called J. Howard's office and was told by Eyvonne Scurlock and Edwin Hunter that there had been a "mis-collation" because everyone

was in a hurry because of J. Howard's impending marriage. (Exs.316, 317.) The alteration of this document demonstrates Hunter's practice of altering documents.

iii. The Donation of the GRAT to the Living Trust (Ex. 268)

The document purports to be dated January 13, 1994. However, Hunter's Billing records indicate that on July 12, 1994, Cherry Doucet of the Hunter Firm "[d]rafted donation of interest in GRAT." (Ex. 649, p. 103, # 7533.) The document also purports to be notarized on January 13, 1994, by Scurlock, yet Scurlock's Notary Book does not include a record of notarizing the document. (Ex. 676.) The GRAT originally provided that if J. Howard died prior to its expiration in 1998, 99% of the MPI shares that it owned would revert to J. Howard's estate, which Pierce and Hunter feared would go to Vickie through a "clandestine California will." By transferring the ownership of the GRAT from J. Howard to the Living Trust, they hoped to insulate the GRAT from ever passing MPI stock to Vickie.[40] Additionally, by back-dating the document, they would insure that it had not been transferred to Vickie while J. Howard was in California.

[40] In May 1995, Pierce and Hunter arranged to sell the GRAT's MPI shares back to MPI for cash, to make absolutely certain that Vickie would never have any MPI stock.

iv. The Promissory Note to MPI, the Pledge, and Assignment of the Pierce Note (Exs.287-289) all of which are dated June 1, 1994

These three documents were in fact signed on July 13 or 15, 1994. Hunter's billing records show that Cherry Doucet of the Hunter Firm "[d]rafted pledge and assignment; Drafted promissory note" on July 11, 1994. (Ex. 649, p. 103, # 7535.) There is no record of a meeting with Pierce or J. Howard to sign these notes on June 1, 1994, or records indicating that Hunter prepared these documents prior to June 1, 1994. Hunter's Fine Tuning Memo, which was drafted after J. Howard's June 27, 1994 marriage to Vickie, indicates that these transactions should occur in the future. (Ex. 310a, p. 6, VII.A.4.) The documents also purport to be notarized on June 1, 1994 by Scurlock, yet Scurlock's Notary Book (Ex. 676) does not include a record of notarizing the documents on June 1, 1994, or at any date thereafter. As noted, *supra,* these documents allowed Pierce, at his discretion, to stop the flow of income from J. Howard, and instead re-direct the payments to MPI. Because the income would have been community property, Vickie had an interest in these notes after she married J. Howard, and thus the backdating deprived her of that interest without her involvement. Additionally, the documents effectively eliminated J. Howard's ability to give or bequeath to Vickie the August 25, 1993 Pierce Note, as it was encumbered by the note to MPI.

v. The Amended and Restated Living Trust of July 13, 1994

The Amended and Restated Living Trust dated July 13, 1994 had key pages substituted. Donald J. Fandry, a forensic document expert, undertook an extensive examination of this document. (AP 023175-023206.) Fandry found that page two was added to the Amended and Restated Living Trust after the date of July 13, 1994. According to Fandry, the second page, where the Living Trust was made irrevocable has a different type of paper with no watermark, whereas the other pages all contain a watermark, "Eatons Eminence bond U.S. Berkshire."

Additionally, Fandry found that the printing on this second page is also a different type of printing process indicating that it was printed at a different time and/or on a different printer. The toner spattering, when inspected under a microscope revealed that the toner is much broader on the watermarked pages. The toner spattering on page two is much cleaner, meaning less spattering of toner.

Finally, Fandry found that the staple hole patterns do not match other pages indicating that pages were substituted subsequent to the initial completion of the document.

Fandry also found that page three of the living trust was substituted. According to Fandry, the staple holes on page three also show a marked discrepancy with other pages. As an example, there are significantly less staple holes on page three than page four.

The indentations of the staple wire patterns are not consistent with other pages. The holes and indentations do not line up.

Another expert, J.L. Hale, Jr., reviewed the Amended and Restated Living Trust Document and came to similar conclusions as Fandry. (Ex. 686.) Hale confirmed that page two has no watermark, that the staple patterns are different from the other pages, and that it was printed with a different quality printer. Hale also points out that page three has staple hole patterns that are inconsistent with the rest of the document. In addition, Hale notes that the watermark on page three is upside-down, indicating that it was inserted into the document at another time than the other pages. According to Hale, "Page 2 was inserted to replace a different page at some point . . . [and it] is patently obvious that page 3 was inserted at some point to replace a different page." (Ex. 686.)

Based on this analysis, and the Court's own review, the Court agrees with both Fandry and Hale that pages two and three were substituted. Pages two and three include Article III, which reads as follows:

> This trust shall be irrevocable. The Settlor expressly reserves the power to substitute E. Pierce Marshall, Elaine T. Marshall, or any § 170(b)(1)(A) organization for the beneficiary of any established in the instrument. For the purposes of this Article III, the term "§ 170(b)(1)(A) organization" shall have the

> meaning attributable to it by the Income Tax Regulation § 1.170 A-G.
>
> Further, Settlor expressly reserves the right to reduce any distributions set forth in Article VI, Paragraph B, any such reduction increasing the portion of the trust estate under Article VI, Paragraph C. Settlor shall exercise these powers by notarial act.
>
> Except as provided in this Article III, the Settlor shall have no power to alter, amend, modify or change this trust indenture.

All statements or references to the Trust being irrevocable are set forth in Article III, which is contained entirely on pages two and three. These pages have been substituted due to intentional acts by Hunter, with the knowledge of Pierce. Moreover, there is no evidence, other than the self-serving statements offered by Pierce and Hunter, that J. Howard had ever before sought to make the Living Trust irrevocable, despite numerous opportunities to do so in the preceding ten years. The trust provisions were read to J. Howard, and the pages containing the irrevocable clause were substituted after the document was executed. Because of these intentional acts, the Court finds that [ ] the original pages set forth a revocable trust.

Fandry and Hale opine that not only does the Amended and Restated Living Trust contain substituted pages, which J. Howard would not have seen, but that in fact, J. Howard's signature on page

twenty-two of the document is forged. Fandry and Hale undertook significant handwriting analysis to determine that the signature of J. Howard was likely not genuine. Moreover, Hale found that the watermark on page twenty-two is also upside-down, corroborating his opinion that J. Howard's signature was forged.

These three pages are the most critical pages in the Amended and Restated Living Trust. Pages two and three make the trust irrevocable, while page twenty-two is the page on which J. Howard purportedly signed the document. These three pages are the only ones that have been drawn into dispute during the course of the litigation between the parties, and are the pages that served to insure that J. Howard could not make a substantial gift of his wealth to Vickie.

It is also clear from the record that the Amended and Restated Living Trust was not immediately recorded. Instead, it was kept in the possession of either Pierce, Hunter or Scurlock for four to six days, until July 19, 1994. At that point, the document was given to Townsend, who returned to Lake Charles with it and subsequently recorded it in Glasscock County, Texas on July 21, 1994.

The testimony of Hunter and Pierce border on a concession of substitution of these pages. The explanation offered by Hunter is that possibly J. Howard himself substituted these two critical pages. There is absolutely no testimony or evidence of anything that

approaches this ludicrous speculation. The suggestion that J. Howard, who had just had this document read privately to him by Hunter, subsequently got his hands on the document and attempted to read the unreadable and then went to a word processor and typed out these new pages and stapled them together is unbelievable. Furthermore, the evidence shows that, up until the time of his death, J. Howard believed the Living Trust was revocable. *See* Part IV.D.5, *supra.*

vi. The Sale for Private Annuity (Ex. 3370)

As detailed, *supra,* this document was signed under false pretenses. Under the terms of the document, in May 1995, J. Howard sold to MPI his remaining shares of MPI stock for an annuity that would not begin paying until March 1996. Hunter represented that this would be a sound business investment if J. Howard lived another five years. However, at the time, J. Howard had been extremely ill and had been hospitalized three times in the previous five months. His health was so poor in January that Townsend began looking into funeral arrangements. Even to the extent that J. Howard recovered after January 1995, it was clear that J. Howard, then ninety years-old, would not live for five years, as he had been diagnosed in April 1995 with terminal stomach cancer.

This document is also a case of self-dealing. Pierce signed the document as co-trustee of the living trust and as President of MPI. Thus, he was improperly involved on both sides of the transaction. Moreover, Pierce was the only one that stood to benefit from the sale. By May 1995, Pierce had become the primary shareholder of MPI. He also stood to receive any outstanding shares then owned by his mother, Eleanor, as the residual beneficiary of her charitable trust. Thus, by having MPI purchase J. Howard's remaining shares, he was becoming the sole shareholder of the company. He was able to do this without paying anything to J. Howard since Pierce knew that J. Howard would not live to collect the proceeds of the annuity.[41] Furthermore, Pierce stripped

[41] There is some evidence that this document, and the entire series of documents executed in late May 1995, may have been backdated. The Charitable Lead Trust is questionable on its face, as it purports to be dated on May 29, 1995, but is notarized by Scurlock three days earlier, on May 26, 1995. (Ex. 99.) Once again, Scurlock's notarization is in question, as there is no May 26, 1995 entry in her notary book. (Ex. 676.) Additionally, Hunter's billing records indicate that his partner, Glynn Blazier, was researching: "requirements of qualified lead annuity trust; Prepare draft documents" on July 12, 1995. (Ex. 3344, p. 80.) Additionally, Pierce had strong motivation to backdate the documents to May 26. On May 31, 1995, Glenn Johnson was appointed J. Howard's temporary guardian ad litem, thus any documents relating to his assets signed after that time might be called into question. The motivation to falsify, the irregularities of the document, the use of a discredited notary, work that appears to relate to the document after it was purportedly signed, and the pattern that Pierce, Hunter and Scurlock have demonstrated in falsifying and backdating documents give strong

(Continued on following page)

him of his last remaining interest in MPI which he could have given to Vickie.

vii. The Renunciation of J. Howard's right to receive distributions from the Living Trust (Ex. 145)

Acting under his power of attorney, Pierce purportedly signed this document for J. Howard on December 28, 1994. However, as demonstrated in Part IV.D.6, *supra,* that claim in not credible and the document is irregular on its face. Pierce's signature purports to be notarized by Eyvonne Scurlock, but there is no such record in her notary book. (Ex. 676.) Moreover, Finley Hilliard's signature as a co-trustee of the Living Trust was not notarized until February 22, 1996, more than six months after J. Howard's death. (Ex. 145.) The document may have been signed in Spring 1995, as part of Pierce's plan to cut Vickie off or in February 1996, after J. Howard's death. Although the Court cannot determine with certainty the date the document was actually signed, it does conclude that it was not signed in December 1994. This left J. Howard without the right to collect any income from his primary assets contained in the Living Trust, and he would therefore be unable to give any of it to Vickie. It also effectively cut-off

indication that these documents were also backdated. However, the evidence on this point is not as clear as the evidence of backdating of the other documents, and is unnecessary to this Court's findings.

Vickie's rights to demand payment from the Living Trust.

viii. The Co-Trustees Resolution, purportedly dated February 7, 1995, that re-sited the trust from Houston, Texas to Calcasieu Parish (Lake Charles), Louisiana (Ex. 341)

Hunter's billing records indicate that work began on changing the situs of the trust on May 31, 1995. (Ex. 3344, p. 64.) On that day, Hunter spoke to Hilliard and Townsend about the issue. (Id.) He then had a conference with his partner Tim O'Dowd on the issue. (Id.) O'Dowd researched the issue on May 31 and June 1, 1995. (Id.) On June 5, 1995, O'Dowd wrote to Pierce on the issue. (Ex. 3344, p. 65.) On June 6, 1995, O'Dowd drafted "Resolution of Trustees for change of situs." (Id.) Thus, although the resolution purports to be dated February 7, 1995, it was in fact executed after June 6, 1995. By re-siting the Living Trust to Louisiana, Vickie would lose the ability to control the venue of the litigation, in favor of what Pierce and Hunter considered a more favorable "hometown."

V. FINDINGS PROPOSED BY THE BANKRUPTCY COURT

Except to the extent that they are inconsistent with the findings of fact set forth in this order, this Court's de novo review upholds the findings of fact

proposed by the bankruptcy court in its October 6, 2000 Original Decision, *Marshall I,* 253 B.R. 550.

CONCLUSIONS OF LAW

I. CAUSE OF ACTION FOR TORTIOUS INTERFERENCE WITH AN *INTER VIVOS* GIFT[42]

The bankruptcy court found that Pierce tortiously interfered with Vickie's expectancy of an *inter vivos* gift. The Texas Supreme Court[43] has never ruled on whether Texas recognizes a cause of action for tortious interference with an *inter vivos* gift. *See Brandes v. Rice Trust, Inc.,* 966 S.W.2d 144, 146 (Tex.App.1998). In the absence of a settled rule of law enunciated by the highest court of the applicable state, a federal court should use its best judgment to predict how the highest state court would rule. *Ins. Co. of the State of*

[42] When conducting a *de novo* review of the bankruptcy court's proposed findings of fact and conclusions of law, a district court must review "those matters to which any party has timely and specifically objected." 28 U.S.C. § 157(c)(1). Pierce filed his brief on the merits on June 25, 2001, and his amended assignments of error on June 27, 2001. Pierce did not object to the bankruptcy court's reading of Texas law. On January 8, 2002, Pierce filed an additional brief on Texas law. That brief was untimely and in contradiction of the Court's August 27, 2001 Order stating that "[b]ecause the parties have already briefed the merits, no trial briefs need be submitted." Accordingly, Pierce's January brief is STRICKEN. Nevertheless, the Court addresses the issue of law *sua sponte.*

[43] Neither side has contended that anything but the law of Texas applies. The Court therefore assumes without deciding that Texas furnishes the applicable law.

Pennsylvania v. Associated Int'l Ins. Co., 922 F.2d 516, 520 (9th Cir.1990). In such a situation, the federal court should look to the decisions of intermediate state courts for guidance. *Id.* "Indeed, state intermediate appellate court decisions are not to be disregarded by a federal court unless it is convinced by other persuasive data that the highest court of the state would decide otherwise." *Id.* (internal quotation marks and citation omitted).

Texas courts have recognized a cause of action for tortious interference with an inheritance. *King v. Acker,* 725 S.W.2d 750, 754 (Tex.App.1987) (citing *Tippett v. Hart,* 497 S.W.2d 606 (Tex.Civ.App.1973)). In finding that the tort existed, the court relied on the ancient maxim that the law will afford a remedy to every invasion of a legal right. *Id.* (citing *Chandler v. Welborn,* 156 Tex. 312, 294 S.W.2d 801, 807 (1956)); *accord Marbury v. Madison,* 5 U.S. (1 Cranch) 137, 163, 2 L.Ed. 60 (1803). It therefore adopted the position of the Second Restatement of Torts, which creates a cause of action against "[o]ne who by fraud, duress, or other tortious means intentionally prevents another from receiving from a third person an inheritance or gift that he would otherwise have received." Rest.2d Torts § 774B (1977). By adopting this position, the Texas court concurred with courts in most jurisdictions that also recognize this tort. Rest.2d Torts § 774B, Reporter's Note (1982 App.).

Pierce suggests that *King* is inapposite because it involved interference with an inheritance, not, as the present case does, interference with an *inter vivos*

gift. However, the court in *King* indicated that the Restatement was the proper rule. *King*, 725 S.W.2d at 754. The same section of the Restatement that creates a cause of action for interference with an inheritance creates a cause of action for interference with a gift. *See* Rest.2d Torts § 774B. The same section should therefore be treated in the same manner. In the absence of a persuasive reason to the contrary, the Court is bound by the court's holding in *King* that Texas law adopts section 774B of the Restatement. *Associated Int'l Ins. Co.*, 922 F.2d at 520.

Pierce argues that public policy counsels against recognizing a tort for interference with a gift, because a thwarted donee can approach the donor to resolve the problem. While that is true as a general rule, in circumstances such as the present one, where the donor dies before the interference is discovered, the intended donee's sole remedy is with the courts. Indeed, public policy suggests that a cause of action for tortious interference with a gift is well founded. If a donor intends to give a gift to a donee during his lifetime, but is thwarted by the residual beneficiary of the donor's estate, equity demands that the heir not benefit from his wrongful conduct.

Accordingly, the Court's best judgment is that Texas law recognizes a cause of action for tortious interference with an *inter vivos* gift.

II. ELEMENTS OF TORTIOUS INTERFERENCE WITH AN *INTER VIVOS* GIFT

Although Texas law does not specify the elements of a cause of action for tortious interference with an expectancy, other jurisdictions have clearly delineated the elements. *See, e.g., Doughty v. Morris,* 117 N.M. 284, 871 P.2d 380, 384 (1994). A plaintiff must prove (1) the existence of an expectancy; (2) a reasonable certainty that the expectancy would have been realized but for the interference; (3) intentional interference with that expectancy; (4) tortious conduct involved with the interference; and (5) damages. *Id.*

A. Existence of an Expectancy

J. Howard made numerous promises to Vickie that she would receive half of what he owned. These include promises on at least three occasions when he proposed to her: when J. Howard purchased the Tomball Ranch; when he purchased the 1992 Mercedes for her; and when he proposed to her in June 1994, which she then accepted. J. Howard made similar promises on other occasions in his proposals to Vickie and protestations of love for her. These promises are corroborated by J. Howard's pattern of wooing Lady Walker with his great wealth, and his proposals to Vickie were witnessed on at least one occasion by Harvey Sorensen.

Pierce argues that Vickie did not have a genuine expectancy of a gift because of various actions and public statements that she made. In particular, Pierce

points to Vickie's appearance on the Howard Stern radio show two days before J. Howard's death. At that time, Vickie stated that she would not be getting anything from J. Howard's will. Not only is this statement technically correct, but it was made as part of a public relations campaign. As Vickie testified to in this Court, she did not want people to think that she had married J. Howard only for his money, as that appearance would harm her public persona and detract from her acting and modeling career. It is therefore entirely reasonable that she misled Howard Stern to improve her public image.

As set forth above, while Vickie may have thought he was prepared to give her half of everything he owned, Vickie's objectively reasonable expectancy, and the amount that J. Howard intended to give her, was half of his "new community." This term was defined by J. Howard as one-half of the growth of his assets during the time of their marriage.

The expectancy is also corroborated by the fact that J. Howard conferred on several occasions with his attorney about ways to make a substantial gift to Vickie, that would provide her with money after his death. This included several potential pre-nuptial agreements that contained gift clauses, his direction to Hunter to draft a "catch-all" trust, and his direction to Sorensen to create a legally enforceable gift of one-half of his new community. It is further corroborated by his knowledge that Vickie's career might be short-lived and he believed her to be "unteachable,"

so it would be necessary to provide for her in retirement.

B. Reasonable Certainty of Realization But For Defendant's Conduct

A plaintiff must establish that there is a reasonable certainty that the gift would have been realized but for the defendant's conduct. The Comment to the Restatement notes that "complete certainty is impossible. It is not required." Rest.2d Torts § 774B, cmt. d. (1977). Instead, the Restatement requires only "proof of a high degree of probability that the" donor would have made the gift absent the defendant's conduct. *Id.* Moreover, "[t]he fact that it was the defendant's tortious act that makes it not possible to prove with certainty may be taken into consideration by the court." *Id.*

Here, Vickie has introduced evidence that shows a high degree of probability that J. Howard would have made a gift to Vickie. He directed two attorneys to prepare documents giving her a substantial gift as early as fall 1992. Although the gift was not feasible at that time due to the gift and generation-skipping tax burdens, there is no evidence that J. Howard ever retreated from his intention to give a gift to Vickie. Once he married her, the gift and generation-skipping tax consequences disappeared, and J. Howard would have been able to make a substantial gift. The evidence shows that through the very end of his life, Vickie was the most important person to J. Howard.

Pictures of them together during Christmas 1994 show an elated J. Howard. Tape recorded statements made by J. Howard in May 1995, less than two months before his death, demonstrate that he still believed that Vickie was "the light of his life," that she had "saved his life," and that he wanted her "to be supported by" him. (Ex. 364.) [ ] His actions seeking to have children with Vickie, either by adopting her son or by conceiving on their own, demonstrate that his commitment to provide for her only increased over time. Indeed, it was J. Howard who aggressively gave money to Vickie. He gave her more than anything she had explicitly asked for.

The evidence also demonstrates that it was Pierce's tortious conduct that makes it impossible to prove with certainty that the gift would have been realized. J. Howard placed a tremendous amount of trust in Pierce and Hunter who participated in acts intentionally designed to prevent J. Howard from giving Vickie a substantial gift or to undermine any will or gift that J. Howard signed when he was out of their presence. They presented documents for his signature which he was unable to read and signed documents on his behalf. Had they acted according to his frequently stated wishes, rather than to protect Pierce's interest in MPI and the valuation of Koch Industries, there is a high probability that J. Howard would have made a substantial gift to Vickie.

C. Intentional Conduct

The evidence shows that Pierce and Hunter began undertaking estate planning transactions for J. Howard soon after they learned that he was seeking to make a substantial gift to her. All of these transactions were intended to drain J. Howard of his assets. Pierce's actions were intended to prevent a gift from being made to Vickie so as to not undermine the low valuations accorded to MPI and Koch stock. Allowing Vickie to have a gift based on the value of Koch stock could undermine his litigation position on the value of Koch stock with the dissident Koch shareholders and the IRS on gift and estate taxes. This would cost Pierce millions of dollars in tax litigation, and potentially endanger the liquidity of MPI. Thus, Pierce's actions were all made with the intention of preventing J. Howard from making a gift to Vickie.

D. Tortious Conduct

A defendant's conduct must be "independently tortious in character." Rest.2d Torts § 774B, cmt. c. Evidence of Pierce's tortious conduct is legion. Acting in concert with Hunter, they backdated documents, altered documents, destroyed documents, suborned falsified notary statements, presented documents to J. Howard under false pretenses, and committed perjury.

E. Damages

1. Entitlement

Vickie was damaged in the amount that J. Howard intended to give her. In December 1992, J. Howard told Harvey Sorensen that he wanted to give Vickie one-half of his "new community." (Ex. 62.) "New community" was a term J. Howard had developed, originally related to his marriage to Betty. He wanted Vickie to share in the growth of the assets that he owned and controlled during the time of their marriage. (Ex. 62.) The primary asset he held was his interest in Koch stock, held through MPI.

MPI holds 862,535 shares of Koch common stock, and has held that stock since at least the late 1980's. Prior to August 1993, when Pierce's string of estate planning changes began, J. Howard owned 164,252 shares of the then 236,440 outstanding shares of MPI stock, or approximately 69.5% of MPI. Vickie is therefore entitled to 69.5% of the appreciation in value of the 862,535 shares of Koch stock between the date that she and J. Howard married on June 27, 1994 and his death on August 4, 1995.

Vickie argues that she is entitled to the appreciation in the value of those shares from December 22, 1992, the date the "New Community Memo" was sent. Vickie claims that memo represented a present intent on J. Howard's part to make a gift to Vickie. However, there is no question that the new community that J. Howard referred to was not actually created until J. Howard married Vickie.

The bankruptcy court awarded Vickie the appreciation from June 1994 to August 1999. Here, the ending date is less clear, because J. Howard's intent was to provide for Vickie in her retirement. Indeed the "New Community Memo" did not envision her being able to redeem the warrants from MPI until 15 years after J. Howard and Eleanor died. Although J. Howard has passed on, Eleanor still lives a vibrant and active life, and the end-date is therefore unascertainable. That, however, cannot serve to benefit Pierce, as equity will not allow a tortfeasor to gain by his own tort. The ending date chosen is necessarily somewhat arbitrary. However, August 1999, just before the trial in this matter, is completely disconnected from J. Howard's intent. August 4, 1995 is a more appropriate date, as that is the date that Vickie's and J. Howard's "new community" ended.

Pierce cites *Jensen v. Jensen,* 665 S.W.2d 107 (Tex.1984), for the proposition that, under Texas law, the appreciation in value of separate property held during marriage remains separate property. Pierce's argument, however, misses the mark. While that is an accurate statement of the law, it is not an accurate statement of the issues involved in this case. Had the appreciation become community property under Texas Law, Vickie would be entitled to half regardless of any tortious activity by Pierce. Here, however, the appreciation is relevant because J. Howard intended to give to Vickie a gift, from his separate property, of half of the appreciation of Koch stock. Pierce's argument is therefore unavailing.

2. Valuation

Determining how much the stock in Koch Industries appreciated between June 27, 1994 and August 4, 1995 is an even more difficult task. Koch is a privately held corporation, thus the Court cannot determine the value based on market trades. Litigation over the value of Koch Industries has consumed the time of many of the individuals involved in this case. Indeed, at one point in 1993, Merrill Lynch estimated that the value of Koch Industries was anywhere between $31.06 per share and $2,391.30 per share. (Ex. 681.)

Placing a value on a privately held corporation in general is a difficult task. Moreover, the Koch philosophy is vastly different from most businesses. Koch gives an extremely low rate of return to its shareholders in dividends, allowing the company to grow more rapidly. While that significantly reduces the present share value, it substantially increases the future value of the stock. The experts here have proffered testimony wildly at odds with each other.

i. Mike Hill

In the bankruptcy proceedings, Pierce offered the expert testimony of Mike Hill to show the valuation of MPI. This testimony was stricken by the bankruptcy court as a sanction for Pierce's discovery abuses, but is considered by this Court. Hill utilized the dividend yield method to calculate MPI's value. According to Hill, this was necessary because of the "onerous minority shareholder oppression options available to

majority shareholders domiciled in the State of Kansas (like Koch . . .)." (AP 017175.) However, by using the dividend yield method, the per share value of a company like Koch – that issues a very small dividend and reinvests its profits – is lower than its "inherent" value.

According to Hill, the per share value of MPI[44] as of the date J. Howard and Vickie married was $31,613,322.10. (AP 017180, 017187.) As of J. Howard's death, Hill valued MPI at $29,703,096.75. Hill's valuation would therefore entitle Vickie to no compensatory damages.

ii. Wayne Elggren

Vickie presented Wayne Elggren as an expert on valuation. Elggren employed the guideline company method, whereby Koch's value was determined by reference to similar public companies in the field. Elggren did not calculate the value of MPI or Koch as of August 4, 1995. Elggren calculated the appreciation of J. Howard's approximately 70% interest in MPI from June 27, 1994 to August 30, 1999 (just before trial commenced in the bankruptcy court) at $899,508,268. The bankruptcy court awarded Vickie

[44] Hill valued MPI, not Koch Industries. However, because Koch Industries stock is the major asset of MPI, determining the growth in Koch Industries can be determined by reference to it. The fact that MPI did not appreciate suggests that neither did Koch.

one-half of this amount, or $449,754,134, as compensatory damages.

iii. IRS Settlement

For several years, the Marshall family interests have been involved in various tax litigation matters with the IRS. The IRS has made an offer to settle those cases. (Ex. 3573.) That settlement includes an imputed value of MPI and Koch stock. These settlement offers provide an additional valuation for Vickie's share of MPI and Koch stock holding. Accordingly, the Court makes the following calculations according to the values imputed by the IRS for Settlement purposes. (Ex. 3573, Schedule 9.)

On June 16, 1994, MPI had 222,535 shares of stock actually outstanding. The IRS value of MPI Voting Stock as of June 16, 1994 was $1,039.92 per share. Therefore, the IRS value of MPI as of June 16, 1994 was $231,418,597.20.[45] Because the IRS offer is premised on valuing MPI at 49% of the value of its Koch stock, the value of the Koch shares held by J. Howard through MPI can be set at $472,282,851.43 by dividing by 0.49.

[45] The amount of outstanding voting and non-voting stock is not clear on the record. However, the voting stock is valued only slightly higher than the non-voting stock. Because of Pierce's tortious and wrongful conduct, the Court draws the inference against him and uses the higher value for its calculation.

On May 26, 1995, MPI had 208,470 shares of stock actually outstanding. The IRS value of MPI Voting Stock as of May 26, 1995 was $1,248.70. Therefore, the IRS value of MPI as of May 26, 1995 was $260,316,489. The value of the Koch stock held by J. Howard through MPI can therefore be set at $531,258,140.82

During the period of time covered by these transactions, MPI's interest in Koch appreciated by $58,975,289.39. The time period covered by these valuations is 344 days. Thus, the average daily appreciation of MPI's interest in Koch stock was approximately $171,439.79. J. Howard and Vickie were married during approximately this same period of time, and it is therefore fair to assume that the rate of appreciation during this period was approximately the same. By extrapolating the appreciation of the stock value during this time, the value according to the IRS settlement offer can be obtained. J. Howard and Vickie were married for 403 days. Thus, by multiplying the average daily appreciation of MPI stock during this period of time by 403 days, the Court finds that the appreciation in the value of MPI's interest in Koch stock was approximately $69,090,237.28.

Absent any fraudulent, wrongful, and tortious transactions, J. Howard would have owned 164,213 shares of MPI stock on June 27, 1994. Absent any fraudulent, wrongful, and tortious transactions, there would have been 236,600 shares of MPI outstanding as of June 27, 1994. Thus, on June 27, 1994, J. Howard would have owned approximately 69.4% of

MPI stock. Absent any fraudulent, wrongful, and tortious transactions, J. Howard's ownership interest in MPI would have been identical at the time of his death on August 4, 1995.[46]

J. Howard's share of the appreciation in the value of MPI would therefore be approximately $47,952,304.03. Vickie is entitled to one-half of J. Howard's share of the appreciation of MPI's interest in Koch stock. Using the IRS Settlement numbers, this amount would be $23,976,152.02.

Although the IRS settlement is a reasonable method for calculating damages, the Court considers it inequitable to do so because it was negotiated by Edwin Hunter. As detailed above, Hunter was a key player in Pierce's tortious interference and the Court has no confidence in his credibility. Accordingly,

[46] The IRS settlement offer reflects several sales of stock by J. Howard to Pierce and sale of stock to MPI to cancel J. Howard's outstanding debt to MPI after August 20, 1993. As set forth above, Pierce's tortious conduct began to effect J. Howard's estate planning transactions in August 1993. Thus, the transactions after that date are tainted by Pierce's fraud, and are discounted by the Court. However, the offer does reflect the distribution to Pierce of 160 shares of MPI stock as compensation. Because Pierce had been receiving MPI stock distributions as part of J. Howard's long-held estate planning, the Court does include that transaction in its calculation. Additionally, the offer reflects a gift by J. Howard to "EM, PM, PM" on December 28, 1993. Because these appear to be legitimate Christmas gifts to J. Howard's family members, the Court does include that transaction in its calculation.

Pierce should not have the benefit of Hunter's efforts in this Court.

iv. Book Value

The book value of MPI's interest in Koch stock is recorded in two credit approval presentations to Texas Commerce Bank. (Exs. 684, 685.) These presentations show a value of MPI's Koch stock of $664.4 million as of December 31, 1994 (Ex. 685) and $780 million as of December 31, 1995. This shows an annual appreciation of $115,600,000 and an average daily appreciation of $316,712.33. Because these valuations were taken near the time of J. Howard's marriage and death, it is fair to assume that the average daily appreciation during this time was the same as that during J. Howard's marriage to Vickie. Thus, the Court can extrapolate the appreciation of MPI's interest in Koch Industries during their marriage at $127,635,068.49. As noted in Part II.E.2.iii, *supra,* J. Howard's ownership interest in this would be approximately 69.4%, or $88,585,534.67. Vickie would be entitled to one-half of this, or $44,292,767.33.

The Court returns to first principles. "Fair Market Value" is defined as "[t]he price that a seller is willing to accept and a buyer is willing to pay on the open market in an arm's-length transaction." Black's Law Dictionary 1549 (7th ed.1999). Thus, while appraisers can estimate value, and several have attempted to do so in this case, the Court recognizes that the only real determination of value is when a

sale takes place. Such a transaction ordinarily takes place after an often prolonged negotiation between buyer and seller, with each side attempting to create the best deal for themselves. Although no such situation presents itself in this case, resorting to the book value gives the Court some indication of the proper amount. The book value of the stock represented the collateral that MPI relied on for its line of credit. J. Howard and Texas Commerce Bank thought that book value was a sufficient valuation for regular business purposes. Pierce continued to rely on this when he took over MPI upon J. Howard's death. Indeed, the reports produced by Texas Commerce bank note that, as a privately held company, access to Koch's audited financial statement is limited and that historically the bank received updates of Koch's financial performance from Pierce. (Exs.684, 685.)[47] Accordingly, the Court accepts the book value of MPI as the appropriate measure of damages to be awarded to Vickie.

The Court finds itself in the quandary of finding that the facts are much more egregious than even the bankruptcy court suspected and found, yet awarding

[47] Pierce contended at trial that based on the collateral of Koch stock, Texas Commerce Bank would agree to expand MPI's line of credit to cover the amount that it would owe to J. Howard between 1996 and 2001 for the sale of the Private Annuity, had he lived. That amount would be approximately $10 million per year, or $50 million between 1996 and 2001. Thus, if Pierce believed that Texas Commerce Bank was willing to extend MPI an additional $50 million line of credit, he must have also placed some reliance on the book value of MPI's Koch stock.

a substantially smaller amount of damages. However, the Court is bound to the facts that show that Vickie is entitled to a smaller, but still substantial, award.

F. Punitive Damages

"On a showing in a tort action that a defendant acted willfully, maliciously, fraudulently, or with gross negligence, there may be a recovery of exemplary damages, in addition to compensatory damages." *King*, 725 S.W.2d at 755; *see also* TexCiv.Prac. & Rem.Code Ann. § 41.003 (Vernon 1997). Willful, malicious, and fraudulent conduct must be shown by clear and convincing evidence. TexCiv.Prac. & Rem.Code Ann. § 41.003(b). Here, the evidence of willfulness, maliciousness, and fraud is overwhelming. Pierce and Hunter engaged in a pattern of deceiving J. Howard for nearly two years. They presented documents under false pretenses, suborned perjured notary oaths, falsified and backdated documents, and altered documents, all with the intent of denying Vickie the gift that J. Howard intended to make to her. Pierce was the primary beneficiary of these acts. Pierce had private investigators follow J. Howard when he left Texas to visit Vickie. In support of their plans, Hunter considered abusing the high office of a federal judge. Pierce's conduct continued even after J. Howard was dead, as he participated in a plan to solicit a federal judge and appears to have altered the Renunciation document in February 1996.

Exemplary damages are levied against a defendant as punishment for outrageous behavior and malicious, fraudulent or other culpable conduct. *Trans. Ins. Co. v. Moriel,* 879 S.W.2d 10, 16 (Tex.1994). Like criminal penalties, the goal of punitive damages is to punish the defendant for his wrongful conduct. *Id.* Pierce now owns and controls all of Trof, Inc., MPI's successor in interest, which includes all the interest in Koch Industries that J. Howard held. MPI was valued at more than $260 million by the IRS six years ago. Furthermore, he holds additional amounts of Koch stock that he received either from J. Howard or acquired in other ways through the years. He also apparently has other significant holdings from his past employment as CEO of Electron Corp., and other interests unknown to the Court. In short, Pierce Marshall is an extremely wealthy individual. Small and nominal amounts will do little to deter wrongful conduct, and a substantial sum is warranted for the pattern of malicious conduct that continued on for several years.

In determining the amount of punitive damages to award, the Court must consider the reprehensibility of the defendant's conduct and the harm inflicted on the defendant, *In re Exxon Valdez,* 270 F.3d 1215, 1240-41 (9th Cir.2001), as well as the defendant's wealth, to determine the appropriate level of punitive damages. Here, the level of misconduct is far worse than even the bankruptcy court, which awarded $25 million in punitive damages, believed was present. The alteration of documents was not

limited to the living trust and the plans to interfere with the administration of federal courts were hidden until discovery was finally extracted. Only because the Court recognizes that the amount of punitive damages must have a rational nexus to the actual damage award does the Court limit the total award to a doubling of the actual damages.

Accordingly, the Court assess punitive damages in the amount of $44,292,767.33.

CONCLUSION

Any conclusion of law erroneously labeled herein as a finding of fact shall be deemed a conclusion of law. Any finding of fact erroneously labeled herein as a conclusion of law shall be deemed a finding of fact.

The Court finds and concludes that Vickie is entitled to judgment against Pierce on her counter-claim for tortious interference with an inter vivos gift, and awards compensatory damages in the sum of $44,292,767.33, plus costs of suit, plus punitive damages in the amount of $44,292,767.33.

IT IS SO ORDERED.

UNITED STATES DISTRICT COURT

FOR THE CENTRAL DISTRICT OF CALIFORNIA

In re	
VICKIE LYNN MARSHALL,	
E. PIERCE MARSHALL,	
Plaintiff,	**CASE NO. SA CV 01-97 DOC**
v.	
VICKIE LYNN MARSHALL,	**(BANKRUPTCY CASE NO. LA 96-12510 SB; ADVERSARY CASE NO. AD 96-1838 SB)**
Defendant.	
VICKIE LYNN MARSHALL,	**JUDGMENT**
Counterclaimant,	(Filed Mar. 7, 2002)
v.	
E. PIERCE MARSHALL,	
Counterdefendant.	

This action came before the Court for a de novo review of the proposed findings of fact and conclusions of law issued by the bankruptcy court after trial in this matter. Beginning on June 25, 2001, this Court conducted a de novo review of the bankruptcy court's proposed findings. From December 11, 2001 to

January 8, 2002, this Court conducted an evidentiary hearing wherein it accepted the testimony of the central figures in the case, documentary evidence, and arguments of counsel. After reviewing all of the evidence in this matter and findings of fact and conclusions of law having been rendered,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED that judgment be entered in favor of Vickie Lynn Marshall and against E. Pierce Marshall, as follows:

1. Vickie Lynn Marshall shall recover from E. Pierce Marshall compensatory damages in the amount of $44,292,767.33.

2. Vickie Lynn Marshall shall recover from E. Pierce Marshall punitive damages in the amount of $44,292,767.33.

3. Vickie Lynn Marshall shall recover costs of suit, to be taxed by the Clerk, in the amount of $

4. E. Pierce Marshall shall recover nothing against Vickie Lynn Marshall.

IT IS SO ORDERED.

DATED: MARCH 7, 2002

/s/ David O. Carter
DAVID O. CARTER
United States
District Judge

271 B.R. 858

UNITED STATES DISTRICT COURT

FOR THE CENTRAL DISTRICT OF CALIFORNIA

In Re	**CASE NO. SA CV 01-97 DOC.**
VICKIE LYNN MARSHALL,	**(BANKRUPTCY CASE NO. LA 96-12510 SB; ADVERSARY CASE NO. AD 96-1838 SB)**
Debtor.	
E. PIERCE MARSHALL,	
Plaintiff,	
v.	
VICKIE LYNN MARSHALL,	**ORDER DENYING COUNTER-DEFENDANT'S MOTION FOR SUMMARY JUDGMENT**
Defendant.	
VICKIE LYNN MARSHALL,	
Counter-claimant,	
v.	(Filed Dec. 21, 2001)
E. PIERCE MARSHALL,	
Counter-Defendant.	

Before the Court is Plaintiff and Cross-Defendant E. Pierce Marshall's (Pierce)[1] motion for summary

[1] As all the principals in this matter share the same last name, the Court will refer to the parties by their given names, as is customary in cases involving family members.

judgment based on res judicata or collateral estoppel. After reviewing the moving, opposing, and replying papers, and for the reasons set forth below, the Court DENIES the motion.

I.

BACKGROUND

Defendant and Cross-Claimant Vickie Lynn Marshall (Vickie) is the surviving widow of J. Howard Marshall II (J. Howard), who died on August 4, 1995. Vickie and J. Howard were married on June 27, 1994, after two and a half years of courtship. At the time of their marriage, Vickie was 26 years old and J. Howard was 89 years old. Vickie, also known as Anna Nicole Smith, is a figure of some notoriety because of her career as a model. Prior to their marriage, J. Howard had assisted in developing her career. J. Howard is also a figure of some notoriety in his own right, as he was said to be either the richest or second-richest man in Texas at the time of his death. His wealth was held in several different ways, including a living trust, and the exact amount and location of his wealth at the time of his death is disputed, but estimates put it at as high as $2 billion.

It is undisputed that J. Howard lavished great sums of money on Vickie during their courtship and marriage. Nonetheless, he did not explicitly provide for Vickie in his will. However, according to Vickie, J. Howard promised Vickie that she would receive substantial wealth and be taken care of. J. Howard,

Sr.'s son from a former marriages, Pierce, contests whether J. Howard ever made such promises.

The magnitude of the sums of money involved in J. Howard's estate has sparked intensely contested litigation on several fronts. First, some probate proceedings took place in Louisiana, but were dismissed some time ago after a jurisdictional ruling by the Louisiana Supreme Court. Second, the estate is currently going through probate in Texas. Trial in the probate proceedings has concluded, and the jury has returned a verdict. Judgment was entered on August 15, 2001. After cross-motions by both Vickie and Pierce, and an order from the bankruptcy court holding that parts of the judgment violated Vickie's discharge in her bankruptcy proceedings, the Texas probate court entered a modified judgment on October 25, 2001. Both sides filed cross-motions for a new trial, and the Texas probate court issued a second modified judgment on December 7, 2001.

Third, on January 25, 1996, a few months after J. Howard's death, Vickie filed for Chapter 11 bankruptcy here in the Central District of California. This bankruptcy case engendered the current adversary proceeding. On May 7, 1996, Pierce filed an adversary complaint seeking a determination that Vickie owed him a debt that was nondischargeable. Pierce alleged that Vickie had defamed him when, prior to the time she filed for bankruptcy and with her complicity, some of her lawyers told members of the press that

Pierce had used forgery, fraud, and overreaching to gain control of Howard's assets.[2] On June 11, 1996, Pierce filed a proof of claim in the bankruptcy case. He made the claim by attaching a copy of the complaint from his adversary proceeding.

Vickie responded to both the adversary complaint and the proof of claim. As to the adversary proceeding, on June 14, 1996 she answered, in part asserting truth as a defense. She also asserted counterclaims for fraudulent transfer, an injunction, conversion, tortious interference with inheritance, breach of fiduciary duty, abuse of process, fraud, promissory estoppel, breach of contract (third-party beneficiary), the imposition of a constructive trust, an accounting, and indemnity and contribution. As to Pierce's proof of claim, Vickie filed an objection on July 3, 1996.

On September 22, 1998, Pierce filed a motion to withdraw the reference for his adversary proceeding. This motion was assigned to Judge Keller for determination. Judge Keller issued a ruling on October 21, 1998, but he then vacated that order and issued a new ruling on March 10, 1999. The March 10, 1999 ruling denied Pierce's request to withdraw the reference. The effect of this ruling was that the Pierce

[2] Debts based on "willful and malicious injury," such as intentional torts, are not dischargeable. 11 U.S.C. § 523(a)(6). Damages for libel or defamation are not dischargeable when the statements were published with knowledge of their falsity. *Wheeler v. Laudani*, 783 F.2d 610, 615 (6th Cir. 1986).

adversary proceeding remained in the bankruptcy court in its entirety.

On November 5, 1999, the bankruptcy court granted summary judgment for Vickie on Pierce's claim. It found that Vickie had published no statements about Pierce, had not ratified any statements about Pierce made by her attorneys, and was not otherwise vicariously liable for any statements her attorneys had made about Pierce. Thus, it held that Vickie had not committed a willful or malicious act under 11 U.S.C. § 523(a)(6).

Vickie's counterclaims against Pierce went to trial in the bankruptcy court in the fall of 1999. Approximately ten months later, on October 6, 2000, the bankruptcy court issued an Amended Memorandum of Decision Following Trial ("Amended Decision"). *In re Vickie Lynn Marshall*, 253 B.R. 550 (Bankr. C.D. Cal. 2000). Based on the evidence at trial and in large part on facts found against Pierce as sanctions for his discovery abuses, the bankruptcy court concluded that Pierce tortiously interfered with Vickie's expectation of an *inter vivos* gift. The bankruptcy court awarded Vickie $449,754,134 in compensatory damages. Subsequently, the bankruptcy court awarded $25 million in punitive damages and issued a judgment. After the judgment was entered in the bankruptcy court, Vickie voluntarily dismissed her claims against Pierce in the Texas probate proceedings for tortious interference with an inheritance or *inter vivos* gift.

Pierce appealed the bankruptcy court's judgment to this Court. On June 19, 2001, this Court entered an Amended Order Regarding Subject Matter Jurisdiction. *Marshall v. Marshall (In re Marshall),* 264 B.R. 609 (C.D. Cal. 2001). The Court reversed the bankruptcy court's ruling that this was a core matter pursuant to 28 U.S.C. § 157. Accordingly, the Court deemed the bankruptcy court's Amended Memorandum of Decision to be proposed findings of fact and conclusions of law pursuant to 28 U.S.C. § 157(c)(1). Consistent with that provision, the Court began to undertake a *de novo* review of the bankruptcy court's proposed findings. On October 5, 2001, this Court held a hearing to review whether the bankruptcy court's evidentiary sanctions were proper.[3] The Court determined that it could not at that point determine that the evidentiary sanctions were appropriate, and therefore would allow additional evidence to be presented at the hearing on the *de novo* review of the merits of Vickie's claim. Pierce was also ordered to produce several hundred boxes of documents subject to previous orders to compel discovery.

Pierce now moves for summary judgment, asserting that Vickie's claims are precluded by the doctrine of claims preclusion by the judgment in the Texas probate proceedings. Alternatively, Pierce asserts that Vickie is estopped from arguing the key elements of

[3] The Court has at times referred to this as the bankruptcy court's Establishment Order.

her claim for tortious interference with an *inter vivos* gift under the doctrine of issue preclusion because of the Texas probate judgment.

II.

DISCUSSION

The Full Faith and Credit Act requires the Court to give state court judgments the same effect as a court of that state would. 28 U.S.C. § 1738.[4] The Court must give preclusive effect to judgments whenever a

[4] This same provision requires that the Texas probate court give full faith and credit to the judgments of federal courts. At oral argument, Pierce represented that Vickie had never requested the Texas probate court give preclusive effect to Vickie's then-operative judgment from the bankruptcy court. That representation was inaccurate. On January 29, 2001, Vickie's Texas counsel requested the Court apply res judicata to the bankruptcy Court's judgment. The Texas probate court held the following exchange:

> **THE COURT**: I don't think I have an obligation to give full faith and credit to a court's jurisdiction after this [the Texas probate case] started. . . .
>
> **MR. CUNNINGHAM** [Vickie's Texas counsel]: The judgment is now final, and the judgment has been appealed, and we are now saying based on that it's entitled to that. . . .

The Court then ruled that Vickie was "not to raise any issue about the California case, whatsoever, in answer to any question, no matter how appropriate she things [sic] that to be. . . ." *See* Statement of Facts (Final Version) 1/29/01 Marshall v. MacIntyre, No. 276,815 (Tex. Probate Harris County), at 29, 48; Testimony from Texas Probate Court Trial, Volume 2 of 3, Testimony of Vickie Marshall.

court of the state that the judgment issued from would give the judgment preclusive effect. *Allen v. McCurry,* 449 U.S. 90, 96, 101 S. Ct. 411, 416 (1990).

> The federal courts have traditionally adhered to the related doctrines of res judicata and collateral estoppel. Under *res judicata,* a final judgment on the merits of an action precludes the parties or their privies from relitigating issues that were or could have been raised in that action. *Cromwell v. County of Sac,* 94 U.S. 351, 352 (1876). Under collateral estoppel, once a court has decided an issue of fact or law necessary to its judgment, that decision may preclude relitigation of the issue in a suit on a different cause of action involving a party to the first case. *Montana v. United States,* 440 U.S. 147, 153, 99 S. Ct. 970, 973 (1979).

Allen, 449 U.S. at 96, 101 S. Ct. at 414-415 (footnote omitted).

A. Res Judicata

The doctrine of *res judicata*[5] does not apply here. Vickie did not litigate, and was not required to bring,

[5] *Res Judicata* is used by different authorities to refer to the preclusive effects of judgments generally, or alternatively as the preclusive effect that a judgment has on other claims that could have been brought in the prior proceeding. This second definition is modernly referred to as claims preclusion. When used in this order, the term *res judicata* shall be deemed to encompass only the doctrine of claims preclusion.

her claim for interference with an *inter vivos* gift in Texas. Texas Rule of Civil Procedure 97, which is nearly identical to Federal Rule of Civil Procedure 13(a), includes four specific exceptions to the compulsory counterclaim requirement, one of those exceptions is that a party need not bring a counterclaim if it is subject to a pending action. Here, Vickie's claim was subject to the present adversary proceeding. It is quite literally hornbook law that "[a] party who fails to interpose a counterclaim that falls under one of these exceptions will not be barred from interposing that claim in future litigation." Charles Alan Wright, Arthur R. Miller, Mary Kay Kane, 6 *Federal Practice and Procedure, Civil* § 1411, at 79 (2d ed. 1990). Because Vickie was not required to bring her claim in the Texas probate court, she cannot now be precluded from litigating it in the bankruptcy proceeding. *See* Tex R. Civ. P. 97; *see also Cromwell,* 94 U.S. at 352. Therefore, only the doctrine of collateral estoppel could apply here.[6]

B. Requirement of a Final Judgment

For both *res judicata* and collateral estoppel, a previous judgment must be final in order to have preclusive effect. *Allen,* 449 U.S. at 96, 101 S. Ct. at 414-415. "In a 1986 landmark case, the Texas Supreme

[6] Collateral estoppel is the doctrine modernly referred to as issue preclusion, and those terms should be considered synonymous for the purpose of this order.

Court adopted the rule of section 13 of the Restatement (Second) of Judgments and held that for *res judicata* and collateral estoppel purposes, judgments become final once the trial court loses plenary power over the judgment." *Gulf Ins. Co. v. Clarke,* 902 S.W.2d 156, 159 (Tex. App. 1995) (citing *Scurlock Oil Co. v. Smithwick,* 724 S.W.2d 1, 6 (Tex. 1986)).

Here, there is no final judgment under Texas law. A judgment is only final once the trial court loses the power to alter or amend the judgment. *Id.* (quoting *Street v. Honorable Second Court of Appeals,* 756 S.W.2d 299, 301 (Tex. 1988)). Under Texas law, a trial court can grant a new trial or amend the judgment if a motion is filed by any party within thirty (30) days of the judgment being signed. Tex. R. Civ. P. 329b(a), (e). The trial court's power to alter the judgment lasts seventy-five (75) days after the motion is filed. Tex. R. Civ. P. 329b(c). Here, the Texas probate court entered its second modified judgment on December 7, 2001. The parties to that action therefore have thirty (30) days in which to file motions for a new trial or motions to amend the judgment, and the Texas probate court would therefore have an additional seventy-five days to rule on those motions. Until that period lapses, the Texas probate court has plenary power to change its judgment, and the judgment is therefore not final for *res judicata* or collateral estoppel purposes under Texas law. *Scurlock Oil,* 724 S.W.2d at 6.

Pierce argues that the Texas probate court's judgment should be considered final because it has consistently denied Vickie's motions for a new trial

and the probate judge has stated that it will deny future motions. As both a matter of fact and law, Pierce is incorrect. As Vickie's counsel points out, paragraph 3.42 of the second modified judgment granted Vickie's request that she not be required to pay temporary administrator fees. Thus, Pierce's bold assertion that she has always been denied relief is incorrect. Although Pierce insists that the Texas probate court will not grant any of Vickie's future motions, this Court will not attempt to prognosticate the actions of other judges.[7] As long as the Texas probate court has plenary power to modify the judgment, it is improper for this Court to assume that it will not use that power.

Because there is no final judgment in the Texas Probate proceeding, it cannot have preclusive effect.

C. Timeliness of Pierce's Motion

Pierce's motion must also be denied because it is untimely. In fact, it is two years late. The trial in this matter was had in the fall of 1999.

Although the evidentiary portion of the Court's *de novo* review has the look and feel of a trial, it is not the trial. The bankruptcy court tried the matter consistent with the provisions of 28 U.S.C. § 157(c)(1).

[7] No doubt Pierce thought that the probate judge would not grant Vickie's motions after it entered its first Modified Judgment.

The Court is now "reviewing *de novo* those matters to which any party has timely and specifically objected." 28 U.S.C. § 157(c)(1). As the Court noted in its August 27 order in this matter, the Court has broad discretion to determine how to go about reviewing the record in this matter, so long as it conducts an actual review. 1 Collier on Bankruptcy ¶ 3.03[3][b]; *Castro v. Perez (In re Castro),* 919 F.2d 107, 108 (9th Cir. 1990). A hearings is not required when reviewing the bankruptcy court's proposed findings of fact and conclusions of law under section 157(c)(1). *See United States v. Remsing,* 874 F.2d 614, 618 (9th Cir. 1989); *see also* 9 Collier on Bankruptcy ¶ 9033.07.

There is no question that this Court could have reviewed the record as submitted in the proceedings below. That, in fact, appears to be the general practice of district courts when reviewing the proposed findings of fact and conclusions of law of a bankruptcy court in a non-core matters. Instead, however, the Court has decided to hold hearings and elicit testimony because of the unusual situation presented in this case. When dealing with the close personal relationships involved here, issues of credibility are central to the case. Moreover, the long and convoluted nature of the record in this case counsels in favor of the Court reviewing evidence directly. Finally, the trial of this matter was governed by evidentiary sanctions against Pierce that essentially determined the questions of liability. Here, however, additional documents have been produced, and the Court has held its decision on sanctions in abeyance. Accordingly, both

sides have been afforded the opportunity to present evidence that was not available in the bankruptcy proceedings. That opportunity, however, does not eliminate the previous proceedings.

At oral argument, Pierce argued that if an appellate court ordered a new trial, then the trial court could give preclusive effect to the judgment of another court entered in the intervening time. The proceedings in this Court, however, are not a trial at all. In a trial, the Court would evaluate the issues anew, without reference to previous proceedings. Here, however, the Court has reviewed the record of the proceedings below. The parties are not required to establish every fact from evidence put in front of this Court, as the Court will rely on evidence adduced in the bankruptcy court. At a trial, the parties would both be afforded the opportunity to put on the entirety of their cases. Here, they are limited to the witnesses that the Court has directed. Testimony from other witnesses is not a matter of right, but will be permitted only in the Court's discretion, based on what it believes is important for reviewing the record.

The Court cannot ignore the fact that the parties have tried this case in the bankruptcy court, nor can its hearings supplant that trial. Doing so would eviscerate the jurisdiction that Congress extended to bankruptcy courts and undermine the scheme for the

efficient resolution of bankruptcy matters that Congress set forth in section 157.[8]

The Court is not aware of any authority, nor does Pierce's counsel point to any, that would support the proposition of applying *res judicata* or collateral estoppel *after* a trial has been had. The reason is obvious. *Res judicata* and collateral estoppel have "the dual purpose[s] of protecting litigants from the burden of relitigating an identical issue with the same party or his privy and of promoting judicial economy by preventing needless litigation." *Parklane Hosiery Co. v. Shore,* 439 U.S. 322, 326, 99 S. Ct. 645, 649 (1979). The Supreme Court, "and other courts have often recognized, *res judicata* and collateral estoppel relieve parties of the cost and vexation of multiple lawsuits, conserve judicial resources, and, by preventing inconsistent decisions, encourage reliance on adjudication." *Allen,* 449 U.S. at 96, 101 S. Ct. at 414-415.

Granting Pierce's motion at this stage, after a full trial had been conducted, would do nothing to further those interests. Once a trial has been conducted,

[8] If anything, when a district court reviews proposed findings of fact and conclusions of law in a non-core matter pursuant to 28 U.S.C § 157(c), the situation is more akin to an appeal. Pleadings and motions regarding the pleadings have been filed. Discovery is taken under the supervision of the bankruptcy judge, dispositive motions are ruled on, issues of law are argued, and eventually evidence is taken. The extraordinary nature of these proceedings does not alter the statutory scheme.

there is no judicial economy to applying *res judicata* or collateral estoppel, no needless litigation has been prevented, few, if any judicial resources have been saved, and the parties have in no way spared themselves (or the courts in three states) of the vexation of multiple lawsuits. A motion to dismiss or to grant summary judgment must therefore be brought before a case has proceeded to trial. Pierce cannot now short-circuit the proceedings under the guise of *res judicata* or collateral estoppel, more than two years after it would be appropriate.[9]

[9] At oral argument, Pierce misapprehended what the Court meant by the issue of timeliness. He argued that collateral estoppel can be raised late in the proceedings, even on appeal. Of course, Pierce does not mean to make the utterly absurd suggestion that a first obtained judgment can be reversed on appeal by an appellate court accepting as established those facts determined at a later trial in another case, and then precluding, *ex post*, the evidence submitted in the first trial. Such a proposition would make every judgment infirm. The Court does not suggest in this order that Pierce has waived his claim by bringing it too late, but only that the judgment on which he relies was rendered too late in the proceedings in this case for collateral estoppel to apply.

The Court is not unmindful of the fact that Pierce could not have brought this motion two years ago, as the probate matter had not even been tried in Texas. That fact, however, does not support Pierce's position, but only furthers the point that in the unusual case where litigation is proceeding simultaneously down two different paths (a situation which is unlikely to arise absent federal bankruptcy jurisdiction), *res judicata* and collateral estoppel are not appropriate and serve only to create a race to judgment.

D. Fundamental Fairness Requires Denying Pierce's Motion

Once Vickie had obtained judgment in the bankruptcy court, she voluntarily dismissed her claims in the Texas Probate proceedings. The bankruptcy court's specifically ordered that her $449 million award be offset by any amount she obtained in the Texas Probate proceedings. She therefore had no motivation to litigate the issues in the Texas Probate proceedings.[10] Binding her now to those findings would be fundamentally unfair.

When dealing with issues of *res judicata* and collateral estoppel, "many of the abstract rules must be informed by a wise sense of real-world affairs and a healthy skepticism about the capacities of any single litigation to settle relationships beyond the immediate dispute." Charles Alan Wright, Arthur R. Miller, Edward H. Cooper, 18 *Federal Practice and Procedure, Juris* § 4400, at 4 (2d ed. 1981). Those remarks are particularly apt when applied to the present case. The real-world considerations lead to the conclusion that Vickie should not be barred from making her arguments in this forum, which was originally chosen by Pierce when he brought his complaint, and which is the only one she has actively sought relief in.

[10] This also raises the question of whether the issues that Pierce seeks to preclude were fully and fairly litigated in the Texas Probate proceedings, a requirement for applying collateral estoppel.

E. Identity of Issues

Pierce cites *Neill v. Yett*, 746 S.W.2d 32, 35 (Tex. App. 1988), for the proposition that the Texas probate court's finding that J. Howard had testamentary capacity and intent, and that Pierce did not exercise undue influence over his father, should bind this Court. *Neill* deals with tortious interference with the expectancy of an inheritance. Vickie's claim, however deals with the interference of an *inter vivos* gift. When dealing with an *inter vivos* gift, the relevant state of mind is not J. Howard's testamentary intent, but his donative intent during his lifetime. Thus, while it might be the province of the Texas probate court to determine what J. Howard intended to do with his estate when he died, the question before this Court is what he intended to do with it while he was still alive.

F. Violation of the Discharge

Vickie finally contends that the Texas Probate judgment violates Vickie's discharge in her bankruptcy proceedings. Both parties agree, although for different reasons, that the bankruptcy court, not this Court, should make that determination in the first instance. That matter is for the bankruptcy court. However, if the judgment is in violation of Vickie's discharge, this Court could not give any preclusive effect to it.

III.

CONCLUSION

Accordingly, Pierce's motion for summary judgment is DENIED.

IT IS SO ORDERED.

DATED: DECEMBER 21, 2001

/s/ David O. Carter
DAVID O. CARTER
United States District Judge

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

CIVIL MINUTES –GENERAL

Case No. SA CV 01-97 DOC Date: September 14, 2001

Title: In Re Vickie Lyn Marshall. E. Pierce Marshall v. Vickie Lynn Marshall; Vickie Lynn Marshall v. E. Pierce Marshall

DOCKET ENTRY

[I hereby certify that this document was served by first class mail or Government messenger service, postage prepaid, to all counsel (or parties) at their respective most recent address of record in this action on this date.)

Date: Deputy Clerk:

PRESENT:

THE HONORABLE DAVID O. CARTER, JUDGE

Kristee Hopkins	Not Present
Courtroom Clerk	Court Reporter

ATTORNEYS PRESENT FOR PLAINTIFFS:	ATTORNEYS PRESENT FOR DEFENDANTS:
NONE PRESENT	NONE PRESENT

PROCEEDING (IN CHAMBERS): DENYING MOTION FOR RECONSIDERATION

Before the Court is Debtor Vickie Lynn Marshall's (Vickie) Motion for Reconsideration of the order holding that her counterclaims are non-core

proceedings. For the reasons set forth below, the Court DENIES the motion.

I. BACKGROUND

On June 19, 2001, the Court issued its Amended Order, holding in part that Vickie's counterclaim for tortious interference with an *inter vivos* gift was a non-core proceeding in the Bankruptcy Court. *See* 28 U.S.C. § 157. Accordingly, the Court held that the Bankruptcy Court's Decision would be treated as proposed findings for *de novo* review by this Court. This eliminated Vickie's judgment against Plaintiff and Counterclaimant E. Pierce Marshall (Pierce). Both sides applied for leave to file an interlocutory appeal of the order with the Ninth Circuit. Vickie now asks for reconsideration.

II. DISCUSSION

In the Bankruptcy proceedings, Pierce filed a proof of claim for defamation, and an adversary complaint for nondischargeability. Vickie's then counterclaimed, initially for interference with an inheritance expectancy and later amended to include interference with an *inter vivos* gift.

Vickie argues now, as she did when the matter was first heard, that her counterclaim was compulsory because it focused on the same set of facts as Pierce's claim for defamation. Pierce's defamation claim was based on arguments that Vickie's lawyers

had made defamatory statements about his alleged interference with the promises made to Vickie by her late husband and Pierce's father, J. Howard Marshall II (J. Howard). Vickie argues that, because proving the truth of those statements would not only be a defense to the defamation claim, but also prove her counterclaim for tortious interference with an *inter vivos* gift, that her counterclaim was compulsory because it arose from the same transaction. Vickie argues that a compulsory counterclaim is, *ipso facto*, a core proceeding.

Vickie focuses on the Court's statement that "Pierce had already obtained a judgment against Vickie's attorneys . . . ." (Am. Order at 25.) Vickie argues that the Court's decision was based on this statement, and therefore Vickie's truth defense would be precluded under the principles of collateral estoppel.

The Court's decision, however, was based on three factors. First, even a compulsory counterclaim is not necessarily a core proceeding in the bankruptcy court because of the limits of the Constitutional limits of a bankruptcy Court's jurisdiction a set forth in the Supreme Court's decision in *Northern Pipeline Const. Co. v. Marathon Pipe Line co.*, 458 U.S. 50, 102 S. Ct. 2858, 73 L. Ed. 2d 598 (1982). (Am. Order at 23.) Second, the fact that Vickie's counterclaim dwarfs Pierce's original claim makes it impossible to find the proceeding core, and thus able to be determined by a non-Article III Court. (Am. Order at 26.) Finally, even though Pierce had not obtained a judgment, Vickie's

primary defense to Pierce's defamation claim, and the theory on which she was granted summary judgment, was that Vickie was not responsible for her lawyer's statements. (Am. Order at 26.)

Thus, even though the Court was mistaken as to the final posture of the case against Vickie's lawyers, the three factors that contributed to the Court's decision are unaffected.

III. CONCLUSION

Accordingly, Vickie's Motion for Reconsideration is DENIED.

The Clerk shall serve this minute order on all parties to the action.

264 B.R. 609

United States District Court, C.D. California.
In re Vickie Lynn MARSHALL, Debtor.
E. Pierce Marshall, Appellant,
v.
Vickie Lynn Marshall, Appellee.
Vickie Lynn Marshall, Cross-Appellant,
v.
E. Pierce Marshall, Cross-Appellee.
No. SA CV 01-97 DOC.
Bankruptcy No. LA-12510 SB.
Adversary No. 96-1838 SB.

June 19, 2001.

Robert E. Mangels, Joseph A. Eisenberg, Herbert A. Bernhard, Julia J. Rider, Jeffer, Mangels, Butler & Marmaro, Los Angeles, CA, G. Eric Brunstad, Jr. Bingham Dana, Hartford, CT, for E. Pierce Marshall.

Rex S. Heinke, Sheila S. Kato, Jessica M. Weisel, Jennifer C. Yang, Greines, Martin, Stein & Richard, Beverly Hills, CA, Philip W. Boesch, Jr., Boesch Law Group, Marina Del Rey, CA, for Vickie Lynn Marshall.

AMENDED *ORDER* REGARDING SUBJECT MATTER JURISDICTION AND WHETHER THE TORTIOUS INTERFERENCE COUNTERCLAIM IS CORE OR NON-CORE

CARTER, District Judge.

In this appeal from the bankruptcy court, a litigant who filed a proof of claim and an adversary

complaint to determine the dischargeability of a debt allegedly owed to him by the debtor challenges a judgment entered against him on a counterclaim brought by the debtor. The debtor also cross-appeals. For the convenience of the Court and the parties, the Court instructed the parties initially to brief only two threshold issues. These issues are whether federal courts lack jurisdiction over this matter because of the probate exception to federal jurisdiction and whether the counterclaim is a core or non-core matter.[1] The bankruptcy court below held that the probate exception does not bar jurisdiction in this case and that the proceeding is a core matter. For the reasons that follow, the Court agrees that federal courts may exercise jurisdiction over this matter, but reverses the bankruptcy court's determination that this is a core matter.

I. BACKGROUND

Appellee and Cross-Appellant Vickie Lynn Marshall ("Vickie")[2] is the surviving widow of J. Howard Marshall II ("J. Howard, Sr."), who died on August 4, 1995. Vickie and J. Howard, Sr. were married on June 27, 1994, after two and a half years of courtship. At the time of their marriage, Vickie was

[1] The Court heard oral argument on these issues on May 7, 2001.

[2] As all the principals in the matters at hand share the same last name, the Court will refer to the parties by their given names, as is customary in cases involving family members.

26 years old and J. Howard, Sr. was 89 years old. Vickie, also known as Anna Nicole Smith, is a figure of some notoriety because of her career as a model. Prior to their marriage, J. Howard, Sr. had assisted in developing her career. J. Howard, Sr. is also a figure of some notoriety in his own right, as he was said to be either the richest or second-richest man in Texas at the time of his death. His wealth was held in several different ways, including a living trust, and the exact amount and location of his wealth at the time of his death appears to be disputed. It seems clear that he was worth at least $1.6 billion.

It is undisputed that J. Howard, Sr. lavished great sums of money on Vickie during their courtship and marriage. Nonetheless, he did not explicitly provide for Vickie in his will. However, according to Vickie, and as found by the bankruptcy court, J. Howard, Sr. promised Vickie that she would receive substantial wealth and be taken care of. J. Howard, Sr.'s sons from two former marriages, J. Howard Marshall III ("J. Howard, Jr.") and Appellant and Cross-Appellee E. Pierce Marshall ("Pierce"), contest whether J. Howard, Sr. ever made such promises.

The magnitude of the sums of money involved in J. Howard, Sr.'s estate has sparked intensely contested litigation on several fronts. First, some probate proceedings took place in Louisiana, but were dismissed some time ago. Second, the estate is currently going through probate in Texas. Trial in the probate proceedings has concluded, and the jury has returned a verdict, but apparently judgment has not yet been

entered. Third, on January 25, 1996, a few months after J. Howard, Sr.'s death, Vickie filed for Chapter 11 bankruptcy here in the Central District of California.[3] This bankruptcy case engendered two adversary proceedings with which this Court has had involvement. This Order refers to these two adversary proceedings as the "Hilliard adversary proceeding" and the "Pierce adversary proceeding."

The Hilliard adversary proceeding began in January 1998 when Vickie filed an adversary complaint against Finley Hilliard as trustee of the J. Howard Marshall Living Trust and as executor of the succession of J. Howard Marshall II, et al. On July 22, 1998, the Honorable William D. Keller issued an order withdrawing the reference to the bankruptcy court of this proceeding, which thereafter proceeded before Judge Keller. On March 10, 1999, Judge Keller stayed the proceeding, pending the outcome of either the Texas probate proceedings or the Pierce adversary proceeding.[4] On November 8, 1999, the proceeding

[3] The bankruptcy court noted in one of its decisions that Vickie apparently filed for bankruptcy because, after not receiving an inheritance from J. Howard, Sr., she lacked money and also because a default judgment had been entered against her on claims brought by her former personal assistant or housekeeper. This claim subsequently settled.

[4] Judge Keller made this ruling in an order entered in case number CV 98-7686 WDK, which was the case number assigned to Pierce's original motion to withdraw the reference of the Pierce adversary proceeding.

was transferred to this Court.[5] The proceeding remains stayed.

The appeal currently before the Court concerns the Pierce adversary proceeding. This proceeding began in 1996, a couple of years prior to the instigation of the Hilliard adversary proceeding. On May 7, 1996, Pierce filed an adversary complaint seeking a determination that Vickie owed him a debt that was non-dischargeable. Pierce alleged that Vickie had defamed him when, prior to the time she filed for bankruptcy and with her complicity, some of her lawyers told members of the press that Pierce had used forgery, fraud, and overreaching to gain control of Howard's assets.[6] On June 11, 1996, Pierce filed a proof of claim in the bankruptcy case. He made the claim by attaching a copy of the complaint from his adversary proceeding.

[5] When it began its existence as an adversary proceeding in the bankruptcy court, the Hilliard adversary proceeding had adversary number AD 98-1159 SB. After the reference was withdrawn but while the Hilliard adversary proceeding was still before Judge Keller, the proceeding had case number CV 98-4398 WDK. After being transferred to this Court, the Hilliard adversary proceeding was assigned case number SA CV 99-1372 DOC. This is the current, operative number for the Hilliard adversary proceeding.

[6] Debts based on "willful and malicious injury," such as intentional torts, are not dischargeable. 11 U.S.C. § 523(a)(6). Damages for libel or defamation are not dischargeable when the statements were published with knowledge of their falsity. *Wheeler v. Laudani*, 783 F.2d 610, 615 (6th Cir.1986).

Vickie responded to both the adversary complaint and the proof of claim. As to the adversary proceeding, on June 14, 1996 she answered, in part asserting truth as a defense. She also asserted counterclaims for fraudulent transfer, an injunction, conversion, tortious interference with inheritance, breach of fiduciary duty, abuse of process, fraud, promissory estoppel, breach of contract (third-party beneficiary), the imposition of a constructive trust, an accounting, and indemnity and contribution. As to Pierce's proof of claim, Vickie filed an objection on July 3, 1996.

On September 22, 1998, Pierce filed a motion to withdraw the reference for his adversary proceeding. This motion was assigned to Judge Keller for determination. Judge Keller issued a ruling on October 21, 1998, but he then vacated that order and issued a new ruling on March 10, 1999. The March 10, 1999 ruling denied Pierce's request to withdraw the reference. The effect of this ruling was that the Pierce adversary proceeding remained in the bankruptcy court in its entirety.[7]

On November 5, 1999, the bankruptcy court granted summary judgment for Vickie on Pierce's claim. It found that Vickie had published no statements

[7] Judge Keller's March 10, 1999 order refers the Pierce adversary proceeding in its entirety back to the bankruptcy court. Specifically, the order states without limitation, "This Court's October 21, 1998 Order is vacated. Accordingly, Case No. CV 98-7686, *In re Vickie Lynn Marshall*, is referred back to the Bankruptcy Court."

about Pierce, had not ratified any statements about Pierce made by her attorneys, and was not otherwise vicariously liable for any statements her attorneys had made about Pierce. Thus, it held that Vickie had not committed a willful or malicious act under 11 U.S.C. § 523(a)(6).

Vickie's counterclaims against Pierce went to trial in the bankruptcy court in the fall of 1999. Approximately ten months later, on September 27, 2000, the bankruptcy court issued a Memorandum of Decision Following Trial ("Original Decision"). The Original Decision held that Pierce tortiously interfered with Vickie's expectation of the inheritance she otherwise could have received through a widow's election. On October 6, 2000, the bankruptcy court issued an Amended Memorandum of Decision Following Trial ("Amended Decision"), which supercedes the Original Decision. *See In re Vickie Lynn Marshall*, 253 B.R. 550 (Bankr.C.D.Cal.2000). Based on the evidence at trial and in large part on facts found against Pierce as sanctions for his discovery abuses, the Amended Decision concludes not that Pierce tortiously interfered with Vickie's expectation of an inheritance, but that he interfered with her expectation of an *inter vivos* gift. Specifically, the Amended Decision states:

> The court finds that Vickie had an expectancy to receive a substantial portion of J. Howard's wealth. J. Howard repeatedly told her that she would receive half of what he owned. While J. Howard never made a will

> with any provision for her, this was because his principal assets were already in the Living Trust. J. Howard's plan was to provide for Vickie from the Living Trust.
>
> In December, 1992 J. Howard instructed both Sorensen and Hunter to arrange a gift to Vickie from the Trust. J. Howard instructed Hunter, a tax and estate planning expert, to prepare a "catch-all trust" for Vickie. A few days later J. Howard instructed Sorensen to prepare the documents for a gift to Vickie of one-half of the future appreciation in J. Howard's interest in MPI stock.[8] No evidence has been offered that these instructions were ever rescinded.

Am. Decision at 7. After discussing the certainty of the gift and Pierce's tortious conduct to prevent it, the Amended Decision then concludes:

> Pierce has tortiously deprived [Vickie] of her expectancy of a substantial *inter vivos* gift from her deceased husband J. Howard.
>
> The court awards damages in the amount of $449,754,134, less any amount that Vickie actually recovers in the pending Probate Court action in Texas. In addition, Vickie is entitled to punitive damages in an amount

[8] MPI, or Marshall Petroleum, Inc., is a privately held corporation that in turn owns stock in Koch Industries, Inc., an oil and gas corporation affiliated with the Marshall family.

> that remains to be determined after her actual damages are calculated.

Am. Decision at 9.

Pierce then filed a motion to withdraw the reference, assigned to this Court for determination. Just prior to argument on that motion, the bankruptcy court issued a third order on November 21, 2000. This decision, the Supplemental Memorandum of Decision Following Trial ("Supplemental Decision"), does not supercede the Amended Decision, but instead supplements it by explaining that the bankruptcy court had determined that Vickie's counterclaims were core proceedings and by imposing punitive damages of $25 million. It requested further briefing regarding certain forms of injunctive relief requested by Vickie, discussed requests by the parties for revisions to its findings of fact and conclusions of law, and set a hearing for December 6, 2000.

This Court heard oral argument on Pierce's motion to withdraw the reference on December 11, 2000 and then took the matter under submission. It then requested further briefing regarding the jurisdictional issue raised by Pierce in his motion.

On December 29, 2000, the bankruptcy court issued an Order on Motion for Entry of Judgment ("Order Re Judgment"). In this order, the bankruptcy court addressed Pierce's contention that the probate exception bars federal jurisdiction over Vickie's counterclaim. The bankruptcy court rejected this contention. It held that Pierce had waived any objections to

jurisdiction and had consented to jurisdiction by filing a proof of claim. Further, it held that in any event, the counterclaim did not fall within the exception, assuming the exception applies to bankruptcy cases. The bankruptcy court also provided further explanation as to why it had determined the matter is a core bankruptcy matter. Finally, the bankruptcy court ruled that it was appropriate to enter final judgment. The bankruptcy court entered a final judgment that day. This appeal followed.

Before considering the appeal, this Court denied as moot Pierce's motion to withdraw the reference, in addition to several motions for leave to file interlocutory appeals filed by Pierce.

II. JURISDICTION AND STANDARD OF REVIEW

The Court has jurisdiction over this appeal pursuant to 28 U.S.C. § 158(a)(1), because the bankruptcy court has entered a final judgment in this adversary proceeding.

The Court reviews the bankruptcy court's legal conclusions *de novo*. Both subject matter jurisdiction and whether a proceeding is core or non-core are legal questions over which the Court exercises *de novo* review. *In re Castlerock Properties*, 781 F.2d 159, 161 (9th Cir.1986) (exercising *de novo* review over

jurisdiction question, including core or non-core classification).[9]

If the Court determines that this is a core matter, it will then review the rest of the bankruptcy court's decision for abuse of discretion. If the Court determines that this is a non-core matter, it will review all aspects of the bankruptcy court's decision, including its factual findings, *de novo*. In non-core matters, the bankruptcy court cannot enter final judgment, and thus if this matter is non-core, the bankruptcy court's decision will be treated as proposed, rather than final.

III. DISCUSSION

Two issues are presented on this first phase of the appeal. First, whether the probate exception to federal subject matter jurisdiction applies to

[9] Vickie notes that a treatise submitted by Pierce as an exhibit states that unless the district court, on a motion to withdraw the reference, makes the determination that a proceeding is core or non-core, the bankruptcy court's determination "will be binding, subject only to conventional appellate review (if permission for interlocutory review is granted under § 158(a)) under the 'clearly erroneous' standard." 1 *Norton Bankruptcy Law and Practice* 2d § 4.26, at 461. This passage is somewhat opaque, is not supported by any citations in the treatise, and is contradicted by the sentence immediately preceding it in the treatise, which states, "The ultimate determination that a proceeding is core is reviewed *de novo*, like other jurisdictional findings." *Id.* at 460. The Court will follow the Ninth Circuit's approach and review the core or non-core determination *de novo*.

bankruptcy proceedings and if so, whether this matter falls within that exception. Second, whether this matter constitutes a core or non-core matter.

In resolving these issues, the Court need consider only the counterclaim actually decided, tortious interference with the expectation of an *inter vivos* gift,[10] rather than all of Vickie's counterclaims. The bankruptcy court issued no ruling in favor of Vickie on any of her other counterclaims, and thus they are not before the Court on this appeal.[11] The theory of the *inter vivos* gift counterclaim is that J. Howard, Sr. placed most of his assets in a living trust prior to his death and that he intended to set up, prior to his death, a structure whereby Vickie would be provided for out of that living trust.

A. Probate Exception

Initially, the Court rejects two of Vickie's arguments. First, Pierce has not waived his objection to

[10] While this counterclaim is titled "Tortious Interference With Inheritance," in the body of the counterclaim it alleges interference with expectancies of "inheritance and/or gift." As indicated, the final decision of the bankruptcy court concerned interference with Vickie's expectancy of a gift from J. Howard, Sr. before his death.

[11] Apparently, at the beginning of the trial in the bankruptcy court, Vickie's attorney stated, "[I]n effect what we're seeking is interference with an inter-vivos gift, we're not seeking interference with inheritance rights because there were no assets left at the time that [J. Howard, Sr.] passed." Vickie's Appendix at 139:2-6.

federal subject matter jurisdiction. While it may be true that it is disfavored for a party to wait until it has lost a case and then assert a lack of subject matter jurisdiction, lack of subject matter jurisdiction is in general a non-waivable defect. Further, while the motion Pierce attempted to bring regarding subject matter jurisdiction was properly rejected by the bankruptcy court for being untimely filed, his answer to Vickie's counterclaim does attack the court's jurisdiction. That the answer does not explicitly use the words "probate exception" is not material, as his answer was sufficient to alert the court and the parties to the fact that he challenged the court's jurisdiction.

Second, the Court rejects the idea that Pierce "consented" to jurisdiction by filing a proof of claim. The notion of jurisdiction by consent, sometimes referred to as jurisdiction "by ambush," was used in bankruptcy law in the past, but the Supreme Court's ruling in *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 102 S.Ct. 2858, 73 L.Ed.2d 598 (1982) seems to contradict it. In addition, in so far as the issue is the actual subject matter jurisdiction of the federal courts, rather than just the bankruptcy court's power to enter a final judgment, such jurisdiction cannot be conferred by consent.

However, considering Pierce's jurisdictional objection on the merits, the Court rejects his position and concludes that federal courts, including both this Court and the bankruptcy court, may properly exercise jurisdiction over this matter.

It is commonly understood that the "probate exception" bars federal courts from probating a will. While at first glance this proposition may seem unremarkable, both the origin and scope of the exception are not entirely clear. As the Seventh Circuit has noted, "The probate exception is one of the most mysterious and esoteric branches of the law of federal jurisdiction." *Dragan v. Miller*, 679 F.2d 712, 713 (7th Cir.1982). In particular, the origins of the exception are rather murky. A historical explanation, involving the exclusive jurisdiction of the ecclesiastical courts in England at the time the Judiciary Act of 1789 was passed, is frequently proffered. *E.g.*, *Markham v. Allen*, 326 U.S. 490, 494, 66 S.Ct. 296, 298, 90 L.Ed. 256 (1946). However, there are potential problems with this explanation. *See Dragan*, 679 F.2d at 713 (describing the historical explanation as "shoddy"). Further, the historical explanation does not offer a compelling reason or rationale for why the exception should be continued today.

Other possible explanations include the idea that probating a will is not a "case or controversy" within the meaning of Article III, or that the Tenth Amendment reserves probate matters to the states. *See Rice v. Rice Found.*, 610 F.2d 471, 475 n. 6 (7th Cir.1979) (Article III); *McCan v. First Nat'l Bank of Portland*, 139 F.Supp. 224, 228 (D.Or.1954) (Tenth Amendment), *aff'd*, 229 F.2d 859 (9th Cir.1956). These rationales may be more satisfying than the historical explanation as justifications for the probate exception today. However, the Supreme Court has never

formally adopted one of these rationales. Also, these rationales conflict with authority that states that the doctrine is "judicially created." *E.g., Rice*, 610 F.2d at 474. If the doctrine stems from the Constitution itself, it is not judicially created.

It is also possible that while not being constitutionally compelled, the doctrine is a result of the principles of comity attendant to our federal system.

The lack of clarity surrounding the origin of the exception makes it difficult to resolve the threshold issue argued by the parties, which is whether the probate exception applies only to diversity jurisdiction or to all federal jurisdiction, including bankruptcy. As Vickie notes, nearly all of the cases applying or analyzing the probate exception arise under diversity jurisdiction. However, this fact alone does not resolve the question, because there are few non-diversity actions in which the issue could even arise. If the exception stems from a historical practice embodied in the diversity jurisdiction statute, it perhaps would apply only to diversity jurisdiction. Similarly, if the exception is just a judicially created doctrine recognizing that the federal interests present in diversity cases are sometimes overshadowed by stronger state interests, it might not apply to cases in which the courts' subject matter jurisdiction derives from federal law, such as bankruptcy law. However, if the exception stems from Article III or the Tenth Amendment, it presumably would apply to any proceeding in federal court, regardless of the basis of the court's subject matter jurisdiction. *Cf. Sutton v.*

English, 246 U.S. 199, 205, 38 S.Ct. 254, 256, 62 L.Ed. 664 (1918) ("[A]s the authority to make wills is derived from the states, and the requirement of probate is but a regulation to make a will effective, matters of strict probate are not within the jurisdiction of courts of the United States.").

Whatever the origin of the exception, the practical and structural considerations attendant to it in the diversity context seem equally likely to arise for any action in federal court, including bankruptcy matters. The legal certainty that is of extra importance when dealing with matters of inheritance, the specialized nature of probate law and the corresponding expertise of probate court, the idea that normally probate matters are of local concern only, and the judicial economy that stem from limiting litigation involving one decedent's estate to one forum, particularly the forum that has asserted *in rem* jurisdiction over the physical property of the decedent's estate, all are still of concern when dealing with bases of federal jurisdiction other than diversity.

Thus, it is the Court's opinion that the exception most likely applies to all matters in federal court, not just those premised on diversity jurisdiction. However, the Court need not formally decide this issue, because even assuming the probate exception applies to this case, the counterclaim decided by the bankruptcy court does not fall within the exception.

In the leading Supreme Court case on the scope of the probate exception, the Court explained:

> It is true that a federal court has no jurisdiction to probate a will or administer an estate. . . . But it has been established by a long series of decisions of this Court that federal courts of equity have jurisdiction to entertain suits in favor of creditors, legatees and heirs and other claimants against a decedent's estate to establish their claims so long as the federal court does not interfere with the probate proceedings or assume general jurisdiction of the probate or control of the property in the custody of the state court.

Markham, 326 U.S. at 494, 66 S.Ct. at 298; *see also Sutton*, 246 U.S. at 205, 38 S.Ct. at 256 (stating that suits that can "be determined without interfering with probate or assuming general administration, are within the jurisdiction of the federal courts").

Here, the bankruptcy court did not assert jurisdiction generally over the probate proceedings for J. Howard, Sr. or take control over his estate's assets, which are a part of the *in rem* jurisdiction of the Texas court administering his probate proceedings. Thus, the probate exception would bar federal jurisdiction over Vickie's counterclaim only if such jurisdiction would "interfere" with the probate proceedings. *Markham*, 326 U.S. at 494, 66 S.Ct. at 298.

Pierce argues that the counterclaim interferes with the Texas probate proceeding because the issues addressed are similar or related. However, courts

hold that a matter must be more than merely related to a probate proceeding to fall within the exception and hence not be within the power of a federal court. The Seventh Circuit has grouped federal courts' decisions regarding the probate exception into two categories. *See Rice*, 610 F.2d at 476. In the first of these categories, the test used is whether the claim rests on an assertion that the will is invalid. *Id.* In the second, the test used is whether under the law of the state administering the probate, the claim could be brought only in the probate court, as opposed to a state court of general jurisdiction. *Id.* The tests are not entirely distinct from each other and courts do not always identify if they are applying one or the other. In substance, both tests are frameworks for analyzing and answering the overarching question, which is whether the assumption of federal jurisdiction will interfere with state probate proceedings. The Ninth Circuit has never explicitly adopted either test.

Under the first test, Vickie's counterclaim for interference with her expectation of an *inter vivos* gift does not fall within the exception. It is uncontested that the counterclaim does not rest on an assertion that J. Howard, Sr.'s will is invalid. On the counterclaim, Vickie makes no assertion regarding the validity of J. Howard, Sr.'s will, which left nothing to her. Whether Pierce interfered with J. Howard, Sr.'s plans to make a gift to Vickie through a trust arrangement is a determination that can be made completely independently from a determination of whether or not J. Howard, Sr.'s will is valid.

Also under the second test, Vickie's counterclaim does not fall within the exception. On the counterclaim, the bankruptcy court found that J. Howard, Sr. intended to give Vickie a gift before he died:[12]

> In December, 1992 J. Howard instructed both Sorensen and Hunter to arrange a gift to Vickie from the Trust. J. Howard instructed Hunter, a tax and estate planning expert, to prepare a "catch-all trust" for Vickie. A few days later J. Howard instructed Sorensen to prepare the documents for a gift to Vickie of one-half of the future appreciation in J. Howard's interest in the MPI stock.

Am. Decision at 7. The bankruptcy court further found that Pierce interfered with J. Howard, Sr.'s plans:

> [Pierce] fired Sorensen for the purpose of preventing him from arranging the gift to Vickie of the increase in value of the MPI stock, and he conspired with Hunter to prevent the preparation of the catch-all trust. . . . [H]e caused the altering of [a document created regarding J. Howard, Sr.'s

[12] The bankruptcy court's factual findings include findings imposed as sanctions for Pierce's discovery abuses. Whether or not these sanctions were warranted and whether or not the bankruptcy court's factual findings were correct are issues that are not before the Court on this phase of this appeal. The Court here considers the findings of the bankruptcy court only as part of its analysis of the nature of Vickie's counterclaim.

> living trust, of which Pierce and his family were the sole beneficiaries] by substituting a new second page of the document after its apparent execution to insert a provision that purported to make the Living Trust irrevocable.

Am. Decision at 8.

Texas law does not require that this counterclaim be asserted in the probate court. Under the Texas Probate Code, a court exercising original probate jurisdiction has exclusive jurisdiction over "applications, petitions and motions regarding probate and administrations." Tex. Prob.Code Ann. § 5(c) (Vernon 1980). Pierce makes no argument that Vickie's counterclaim falls within this provision. Over other matters, probate courts and Texas courts of general jurisdiction, which in Texas are called district courts,[13] have concurrent jurisdiction. For example, probate courts and district courts have concurrent jurisdiction over "actions involving an *inter vivos* trust." Tex. Prob.Code Ann. §§ 5(d), 5A(c)(2) (Vernon 1980). However, there is a further provision regarding matters, such as Vickie's counterclaim, that are within the concurrent jurisdiction of both the probate and district courts. "In situations where the jurisdiction of a statutory probate court is concurrent with that of a

[13] Texas state district courts are of course separate and distinct from the United States District Courts in Texas. Throughout this section of this order, "district court" refers to a Texas state court of general jurisdiction, not a federal court.

district court, any cause of action appertaining to estates or incident to an estate shall be brought in a statutory probate court rather than in the district court." Tex. Prob.Code Ann. § 5A(b) (Vernon 1980). Pierce contends that this provision means that Vickie's counterclaim could not have been asserted in a Texas district court because, in Pierce's view, the counterclaim is a matter "appertaining to" or "incident to an estate."

The Texas Probate Code defines "appertaining to estates" and "incident to an estate" to include:

> [T]he probate of wills, the issuance of letters testamentary and of administration, and the determination of heirship, and also . . . all claims by or against an estate, all actions for trial of title to land and for the enforcement of liens thereon, all actions for trial of the right of property, all actions to construe wills, the interpretation and administration of testamentary trusts and the applying of constructive trusts, and generally all matters relating to the settlement, partition, and distribution of estates of deceased persons.

Tex. Prob.Code Ann. § 5A(b) (Vernon 1980). It is uncontested that Vickie's counterclaim does not fall into any of these specific categories except possibly the last, "generally all matters relating to the settlement, partition, and distribution of estates of deceased persons." However, this is not an exclusive list, and thus even a matter not falling within one of the

specifically enumerated categories could nonetheless be appertaining or incident to an estate.

However, Texas case law confirms that Vickie's counterclaim, under Texas law, is not appertaining or incident to J. Howard, Sr.'s estate. Texas courts hold that "[a]n action is 'incident or appertaining' to an estate when the outcome will have a direct bearing on the assimilation, collection, and distribution of the decedent's estate." *Falderbaum v. Lowe*, 964 S.W.2d 744, 747 (Tex.App.1998); *see also Crawford v. Williams*, 797 S.W.2d 184, 185 (Tex.App.1990) ("Matters incident to an estate includes those matters in which the controlling issue is the settlement, partition, or distribution of an estate."). Here, Vickie's counterclaim is asserted against Pierce individually and makes no claim against the estate or even against the trusts existing at the time of J. Howard, Sr.'s death. In fact, Vickie's counterclaim is at least in part premised on the theory that she is entitled to nothing either from the living trusts or from the estate itself. Her theory is that Pierce prevented J. Howard, Sr. from including her in the living trusts. Thus, it is entirely possible that the trusts, as currently structured, are legally valid but also that Pierce owes Vickie damages for preventing J. Howard, Sr. from structuring the trusts in another way.

The Texas cases cited by Pierce are inapposite because they concern claims regarding an estate itself, rather than against a person individually for actions taken prior to the decedent's death. *E.g., Bailey v. Cherokee County Appraisal Dist.*, 862 S.W.2d 581, 585

(Tex.1993) (holding that taxes accruing on estate property after death are a claim against the estate and that a suit to collect them is therefore "incident to an estate"); *Perfect Union Lodge No. 10 v. Interfirst Bank of San Antonio*, 748 S.W.2d 218, 221 (Tex.1988) (holding that the interpretation of a testamentary trust is "incident to an estate"); *In the Matter of the Estate of McGarr*, 10 S.W.3d 373, 379 (Tex.App.1999) (holding that an action seeking an inventory, accounting, and distribution of an estate was "appertaining to an estate"); *Crawford*, 797 S.W.2d at 185-86 (holding that an action for turnover of estate property, an accounting, a declaration that a will was void for undue influence, and distribution as if the decedent had died intestate had to be brought in the probate court); *Boman v. Howell*, 618 S.W.2d 913, 915-16 (Tex.Civ.App.1981) (holding that a suit seeking declaratory judgment regarding the construction of a will had to be brought in the probate court); *Thomas v. Tollon*, 609 S.W.2d 859, 860 (Tex.Civ.App.1980) (holding that a suit seeking division of an estate was "incident to an estate").

These cases nicely set forth the rule that claims for matters incident to an estate should be brought in the probate proceeding, but they do not address the underlying question of whether Vickie's counterclaim constitutes a matter "incident to an estate." Pierce assumes this to be true without providing authority or argument in support of his position.

Other cases demonstrate that Vickie's counterclaim is not "incident to an estate." In *Sobel v. Taylor*,

640 S.W.2d 704, 706 (Tex.App.1982), one child of a decedent sued his two siblings, also children of the decedent, for alleged misdeeds both as co-trustees of the decedent's trust before his death and as co-executors after the decedent's death. The allegations were similar to those Vickie has made against Pierce: mismanagement of the trust, fraud, and self-dealing. *Id.* The Court of Appeals of Texas held that the suit was not "incident to an estate," and therefore could proceed independently in the district court, rather than the probate court, because the alleged actions occurred prior to the decedent's death and because the damages sought were from the co-trustees and co-executors in their individual capacities, rather than a distribution from the trust itself or the decedent's estate. *Id.* at 707. The same is true of Vickie's counterclaim.

Similarly, in *Jansen v. Fitzpatrick*, 14 S.W.3d 426, 434 (Tex.App.2000), the court held that the district court had jurisdiction over claims more directly related to a probate proceeding than is Vickie's counterclaim. The decedent in *Jansen* had prepared a will naming certain individuals as residuary beneficiaries who, under the will, would receive shares in certain real property owned by the decedent. *Id.* at 429. Subsequent to the preparation of this will and two months before her death, the decedent gave the real property to her niece. *Id.* After the decedent's death, the residuary beneficiaries sued the niece in district court, seeking to have the deathbed conveyance set aside on the grounds that the decedent

was incompetent at the time she made the conveyance and under the undue influence of the niece. *Id.* at 430. The district court's jurisdiction was upheld by the court of appeals, although it was challenged on grounds other than those at issue here. *Id.* at 432-33.

Pierce attempts to distinguish *Sobel* and *Jansen* on the grounds that those suits were against executors and a specific provision of the Texas Probate Code provides for concurrent jurisdiction over actions against executors. *See* Tex. Prob.Code Ann. § 5(d) (Vernon 1980). However, neither the *Sobel* nor *Jansen* court relied on this provision in analyzing whether the claims at issue were "incident to an estate." Further, the statutory provision cited by Pierce also provides for concurrent jurisdiction over actions "involving an *inter vivos* trust," and under Pierce's characterization of Vickie's counterclaim, which differs from the Court's, her claim would fall within this provision.

Pierce also argues that Texas's "dominant jurisdiction" theory, under which the first court to assert jurisdiction over a matter exercises that jurisdiction to the exclusion of all other courts, means that once the Texas probate proceeding was pending, no Texas district court could have heard Vickie's counterclaim. However, this rule is subordinate to the test for whether an action is appertaining or incident to an estate. Thus, if an action is appertaining or incident to an estate and a probate proceeding is pending, under the doctrine of dominant jurisdiction no other court can exercise jurisdiction over matters appertaining or

incident to the estate. However, other courts may exercise jurisdiction over matters that are not incident to the estate. *See Falderbaum*, 964 S.W.2d at 747 (holding that a district court "was not required to abate" an action brought under concurrent probate and district court jurisdiction because the action was not incident to the estate). Here, under the authority of *Sobel*, Vickie's counterclaim is not incident to J. Howard, Sr.'s estate, and hence the dominant jurisdiction doctrine does not apply to it.

Finally, Pierce also notes that under Texas law, a probate court may in some settings have the power to draw in an action pending in a district court on a transfer. Tex. Prob.Code Ann. § 5B (Vernon 1980). However, this provision is irrelevant both because such a transfer can be done only for matters incident to an estate and because that power does not negate the fact that if, for whatever reason, the probate court does not transfer in the action, the district court may continue to exercise jurisdiction over it.

Because, under Texas law, Vickie's counterclaim for tortious interference does not fall within the exclusive jurisdiction of a probate court, it does not fall within the probate exception to federal jurisdiction. Therefore, both the bankruptcy court and this Court have valid subject matter jurisdiction over this counterclaim.[14]

[14] Similarly, but considering Florida rather than Texas law, another federal court held that the probate exception did not bar

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B. Core Versus Non-Core Distinction

Bankruptcy courts may exercise plenary powers only over "core" bankruptcy matters. Over matters that are not core, bankruptcy courts may not enter final judgment, but may only issue proposed findings of fact and conclusions of law. These are reviewed *de novo* by the district court, which then enters final judgment. The bankruptcy court determined that Vickie's counterclaim is a core matter. Pierce disputes this determination.[15]

As in the preceding discussion of jurisdiction, the Court rejects Vickie's suggestion that merely by filing a proof of claim, Pierce subjected himself to the bankruptcy court for all purposes. This theory does not appear to be to the current state of the law. First, the nature of Pierce's claim against Vickie must be analyzed separately from Vickie's counterclaim against Pierce. Otherwise, the body of law that has

federal courts from exercising jurisdiction over a claim for tortious interference with the expectation of an inheritance or gift when the plaintiffs alleged that the defendants "systemically and fraudulently acted to influence one Arthur Welch to revoke a last will and testament in which he had named the [plaintiffs] as substantial beneficiaries and to execute instead a will for the benefit of [defendants]." *DeWitt v. Duce*, 599 F.2d 676, 677 (5th Cir.1979).

[15] If Pierce is correct, this Court will exercise *de novo* review over the other aspects of the bankruptcy court's decision, which are not addressed in this order. If the bankruptcy court and Vickie are correct, this Court will review the other aspects of the bankruptcy court's decision for abuse of discretion.

developed for analyzing counterclaims would be superfluous. Second, whether or not a certain proceeding is core or non-core is a legal question dependant on the issues raised and the procedural posture of the proceeding; a proceeding cannot be transformed from being non-core to being core through consent or waiver. It would go against *Marathon* to hold that by filing a proof of claim, a creditor consents or waives any objections to core treatment.[16] Consent is relevant to the discussion only in that a party may consent to the bankruptcy court issuing final judgment in a non-core matter, thereby rendering any distinction between whether that proceeding is core or non-core meaningless. However, such consent must be express, not implied. Fed. R. Bankr. P. 7012(b). While he failed either to admit or deny that Vickie's counterclaims are core in his answer, Pierce has never expressly consented to the bankruptcy court entering final judgment.[17]

[16] Vickie argues that *Langenkamp v. Culp*, 498 U.S. 42, 44, 111 S.Ct. 330, 331, 112 L.Ed.2d 343 (1990) supports her position. In that case, decided after *Marathon*, the Supreme Court held that after a creditor files a proof of claim, a preferential transfer action asserted in response by the debtor becomes a part of the allowance or disallowance of that claim and there therefore is no right to a jury trial. However, the Court framed the issue in terms of the nature of the claims, not consent. *Id.*

[17] Pierce's attorney once stated at a hearing in the bankruptcy court that Pierce would be "happy" and "pleased" to litigate in the bankruptcy court. Pierce's Appendix at 190-95. The most logical interpretation of these statements, in the context in which they were made, is that he was referring only to litigation

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Initially, Pierce argues that 28 U.S.C. § 157(b), which identifies certain types of proceedings as core, is not "jurisdictional." The word "jurisdiction," which is used in different ways in different contexts, has three relevant meanings or applications in the bankruptcy context. First, a characteristic that would deprive all federal courts of subject matter jurisdiction, such as the probate exception, deprives bankruptcy courts of subject matter jurisdiction. Second, bankruptcy courts, as adjuncts to the district courts, may only exercise "jurisdiction" over the matters given to them by statute. *See* 28 U.S.C. § 1334. Jurisdiction in this second sense of the word is quite broad, covering all core matters and all non-core, "related" matters, but some matters may involve the debtor or the bankruptcy proceeding so tangentially that they are not even "related to" the bankruptcy case. Third, in so far as the word "jurisdiction" is used to mean the bankruptcy court's power to enter a final judgment, the bankruptcy court does not have "jurisdiction" to enter final judgments in non-core matters. However, while a bankruptcy court may not enter final judgment in a non-core matter, it may certainly exercise "jurisdiction" over the matter in the sense of hearing and presiding over the matter up to the point when it presents proposed findings of fact and conclusions of law to the district court.

of Pierce's claim and the dischargeability determination, not to Vickie's counterclaim.

Thus, Pierce's argument that § 157(b) is not "jurisdictional" is true in a certain sense but is somewhat beside the point. Section 157 governs the determination of whether a matter is core or non-core. The bankruptcy court has jurisdiction over both core and non-core matters. Having determined that Vickie's counterclaim does not fall within the probate exception to federal subject matter jurisdiction, the Court has disposed of all "jurisdictional" objections to this case. This is so because, at the least, Vickie's counterclaim is "related to" Vickie's bankruptcy case. "Related to" jurisdiction is very broad, covering any matter that "conceivably" could have an impact on the estate or the administration of it. *In the Matter of Wood*, 825 F.2d 90, 93 (5th Cir.1987). Vickie's counterclaim could have an impact on the estate as it could greatly increase the size of the estate.

However, for the reasons that follow, while it is a "related" matter, Vickie's counterclaim is not a core bankruptcy proceeding.

Any discussion of the distinction between core and non-core matters must start with the Supreme Court's decision in *Marathon*. In this case, the Supreme Court considered the constitutionality of the Bankruptcy Act of 1978, the precursor to the modern bankruptcy code. A plurality of the Court held that it was unconstitutional to vest full and final authority over any matter conceivably related to a bankruptcy case in non-Article III judges, because under the Constitution, the "judicial power" of the United States, if vested in lower federal courts at all, must be vested in

courts with Article III safeguards. *Marathon*, 458 U.S. at 84-87, 102 S.Ct. at 2878-80. Because of its Article I power to determine the substantive components of bankruptcy law, Congress may provide that bankruptcy judges can exercise full authority over those bankruptcy proceedings that are so closely related to substantive bankruptcy law and procedures that they can be said to be "core" bankruptcy matters. *Id.* However, Congress may not, through statutory enactments, give Article I bankruptcy judges the power to render final judgments over matters that are not directly connected to the bankruptcy code. *Id.*

The modern bankruptcy code's distinction between core and non-core "related" matters is a direct response to the constitutional concerns addressed in *Marathon*. Specifically, the code provides:

> Bankruptcy judges may hear and determine all cases under title 11 and all core proceedings arising under title 11, or arising in a case under title 11 . . . and may enter appropriate orders and judgments, subject to [appellate] review under section 158 of this title.

28 U.S.C. § 157(b)(1). Thus, Congress defined "core" matters as "cases under title 11" and "core proceedings arising under title 11[ ] or . . . in a case under title 11." *Id.* The legislative history indicates that through this definition, Congress intended for bankruptcy judges to exercise final authority over as many matters as constitutionally possible.

Proceedings "arising under" title 11 are those substantive claims for relief that are based on rights expressly granted by title 11, the bankruptcy code. *In the Matter of Wood*, 825 F.2d at 96. This provision functions analogously to 28 U.S.C. § 1331, which grants federal courts jurisdiction over claims "arising under" the Constitution or laws of the United States. *Id.*; *see also* 1 Lawrence P. King, *Collier on Bankruptcy* ¶ 3.01[4][c][i] (15th ed.2000). Proceedings "arising in" a case under title 11 are procedural actions that could only happen in a bankruptcy case. The Fifth Circuit has explained:

> The meaning of "arising in" proceedings is less clear, but seems to be a reference to those "administrative" matters that arise *only* in bankruptcy cases. In other words, "arising in" proceedings are those that are not based on any right expressly created by title 11, but nevertheless, would have no existence outside of the bankruptcy.

In the Matter of Wood, 825 F.2d at 97; *see also Collier, supra* ¶ 3.01[4][c][iv] (referring to actions "arising in" as a "residual category").

Both "arising under" and "arising in" proceedings can be distinguished from proceedings that are only "related to" the bankruptcy case. "Related to" proceedings are substantive claims for relief based upon non-bankruptcy law that could have been the subject of an independent lawsuit absent the filing of a bankruptcy case. *Collier, supra* ¶ 3.01[4][c][iv]. In general, the distinction is stated as follows: if a cause of action

is not dependant on the bankruptcy code for its existence, but could have been asserted as an independent lawsuit absent the filing of a bankruptcy case, it is a non-core, related matter. *In the Matter of Wood*, 825 F.2d at 96-97. This distinction stems from the constitutional requirements set forth in *Marathon*.

Considering these general definitions of "core" and "arising under" and "arising in," Vickie's counterclaim appears to be non-core. Substantively, the counterclaim is based entirely on state law. If she had not filed for bankruptcy, she could have asserted the counterclaim in an independent lawsuit against Pierce. Her counterclaim is not based on a right granted by bankruptcy law.

The analysis cannot end here, however. Many of the claims that are litigated in a bankruptcy case could have been separate lawsuits if no bankruptcy petition had ever been filed. This alone does not render the claims non-core, because such a result would eviscerate most of bankruptcy law itself. As stated by Representative Kastenmeier in the legislative history:

> State law rights arising in core bankruptcy proceedings are functionally equivalent to congressionally created rights, because Congress has the power to modify State law rights in bankruptcy proceedings. Unlike the States, Congress may impair the obligations of contracts through the bankruptcy clause. Indeed, the very purpose of bankruptcy is to

> modify the rights of debtors and creditors, and the bankruptcy code authorizes the bankruptcy court to abrogate or modify State-created obligations in many ways.

130 Cong. Rec. H1110 (daily ed. Mar. 20, 1987) (quoted in *Collier, supra* ¶ 3.02[2]). Thus, in determining whether a claim is core or non-core, courts must consider both the substantive nature of the claim and the procedural posture whereby it is asserted. For example, the filing of a proof of claim creates a bankruptcy core proceeding even though the underlying state law claim would not have been. *In re Bellucci*, 119 B.R. 763 (Bankr.E.D.Cal.1990).

In making this analysis of both the substantive and procedural aspects of the proceedings at issue, courts look to 28 U.S.C. § 157(b)(2), in which Congress set forth a list of specific matters it viewed as core.[18] The only provision of § 157(b)(2) that is relevant to Vickie's counterclaim is § 157(b)(2)(C), which states that "counterclaims by the [debtor's] estate against persons filing claims against the [debtor's] estate" are core proceedings.[19] Counterclaims can be

[18] Proceedings not specifically listed in the statute may still be considered core. The statute itself has a "catch-all" provision, and also it states that core proceedings "include" those specifically enumerated. 28 U.S.C. § 157(b)(2).

[19] Vickie also argues that her counterclaim is core as a turnover proceeding under 28 U.S.C. § 157(b)(2)(E). However, the counterclaim ruled on by the bankruptcy court addressed whether Pierce owes Vickie damages in an individual capacity and did not address, for example, turnover of community

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core under this definition when they "arise in" a bankruptcy case. The bankruptcy court held that because of this provision, Vickie's counterclaim is core.

On first impression, the bankruptcy court's decision appears correct. First, the Court agrees with the bankruptcy court that Vickie's counterclaims are not rendered outside the scope of § 157(b)(2)(C) solely because they were brought against Pierce's adversary complaint, rather than against his actual proof of claim. The Pierce adversary proceeding began with an adversary complaint filed by Pierce seeking a determination of dischargeability and a proof of claim, which stated that the amount of his damages was "unliquidated" and to which was attached a copy of his nondischargeability adversary complaint. Vickie answered the complaint and filed counterclaims against it, and she objected to the proof of claim. Numerous courts have found claims asserted by the debtor against a person who has filed proofs of claims against the estate to be counterclaims within the meaning of this section, and therefore core proceedings, even though the claims were asserted by procedures other than counterclaiming against the proof of claim itself. *See, e.g., In re Carrington Gardens Assocs.*, 248 B.R. 752, 766-67 (Bankr.E.D.Va.2000) (holding that a creditor had "waived its right to limit

property already belonging to Vickie. Therefore, the counterclaim cannot be characterized as a turnover proceeding and cannot receive core treatment on that grounds. *In re Kincaid*, 917 F.2d 1162, 1165 (9th Cir.1990).

or bar the bankruptcy court from hearing counterclaims to" its proof of claim against the debtor because, "[b]y filing its proof of claim," it "in essence converted [the debtor's] adversary proceeding . . . [to] a counter claim").[20]

Second, the Court rejects Pierce's argument that he sought only a determination of dischargeability and did not actually make a claim against Vickie's estate. It is true that a nondischargeability complaint does not automatically include or subsume the underlying claim but is instead a separate, theoretically distinct claim. *In re Thrall*, 196 B.R. 959, 967-68 (Bankr.D.Colo.1996). However, here Pierce filed a proof of claim in addition to his nondischargeability complaint. On that proof of claim, he stated that he had a claim for an "unliquidated" amount. He nonsuited Vickie from his then-pending state court defamation action, and he never sought relief from the

[20] For similar cases, see *In re Performance Nutrition, Inc.*, 239 B.R. 93, 99 (Bankr.N.D.Tex.1999) (holding that claims in a bankruptcy trustee's adversary complaint against two persons who had filed proofs of claims against the estate were counterclaims); *Allen v. City Finance Co.*, 224 B.R. 347, 352 (S.D.Miss.1998) (holding that claims asserted in a complaint filed by the debtor against a creditor who had filed proofs of claim "were, in essence," counterclaims against the creditor); *see also Pan American World Airways, Inc. v. Evergreen Intern. Airlines, Inc.*, 132 B.R. 4, 7 (S.D.N.Y.1991) (holding that claims in a complaint initiated by the debtor against an entity that had not yet filed a proof of claim in the bankruptcy proceeding, but intended to do so, were counterclaims within the meaning of § 157(b)(2)(C)).

automatic stay. As his counsel explained at a hearing in the bankruptcy court on a motion brought by Pierce to dismiss or stay Vickie's counterclaims, Pierce "took" his substantive defamation claim and "put" it into the form of the nondischargeability adversary complaint:

> A lawsuit for libel or slander was filed prepetition in Dallas County. The Debtor filed bankruptcy in January. And that matter was stayed. The trial counsel nonsuited the Debtor. We took the claims against the Debtor that were set forth in the . . . slander action, put them into a nondischargeability complaint – . . . . So the allegations that formed the state court petition for libel and slander, as they related to the Debtor, were then taken and put into the nondischargeability complaint, which we filed here in this Court. Now, it was filed as a nondischargeability complaint because we believe that there's evidence to demonstrate [that Vickie acted willfully and maliciously]. So, under 523, it was like a dischargeability complaint and it was filed here.

Vickie's Appendix, Tab 7, at 4:8-14; 6:14-7:1. Later in the same hearing, Pierce's counsel stated that he "has assumed . . . that if the Court was going to stay the counterclaims, you would have stayed the entire adversary proceeding, *which included the slander lawsuit* that was filed under 523. . . . [W]e'd be happy to stay *both halves* of the action. . . ." *Id.* at 20:17-25 (emphasis added). Thus, given that he filed a proof of

claim in addition to his nondischargeability adversary complaint, and given that he never tried to continue to pursue the substantive aspect of his defamation claim against Vickie elsewhere, Pierce cannot now argue that he never made a claim against her estate.

Thus, Vickie's counterclaim for tortious interference falls within the literal language of § 157(b)(2)(C). However, most courts agree that the plain language of § 157(b)(2)(C) cannot be the end of the analysis, because such a construction would conflict with *Marathon*. In the statute, Congress set forth its view as to what matters fall within the constitutional parameters, but in interpreting the statute, courts must consider not just the literal language of the statute, but the constitutional concerns behind it. *In re Castlerock Properties*, 781 F.2d 159, 162 (9th Cir.1986). Specifically as to § 157(b)(2)(c), footnote 31 of the plurality opinion in *Marathon* suggests that it would be unconstitutional to hold that any and all counterclaims are core and therefore can be finally determined by a bankruptcy judge. *Marathon*, 458 U.S. at 79 n. 31, 102 S.Ct. at 2876 n. 31.

Thus, on the one hand, calling any counterclaim that falls within the literal language of the statute core seems to contradict the holding of *Marathon*. On the other hand, calling any counterclaim that could have been asserted as an independent lawsuit noncore seems to render § 157(b)(2)(c) itself nugatory, because any counterclaim could have been asserted as a separate lawsuit absent the filing of the bankruptcy petition. *Collier* notes this problem and states

that "[t]he matter is still unsettled." *Collier, supra* ¶ 3.02[3][d][i].

It appears that the justification for core treatment for counterclaims is a combination of judicial economy and efficiency for the litigants, in addition to recognition of the fact that practically, adjudication of a counterclaim that is closely related to a claim will almost merge into allowance or disallowance of the claim itself. *In re Castlerock*, 781 F.2d at 162.[21] Keeping these concerns in mind, courts have developed various doctrines for limiting the reach of § 157(b)(2)(C). For example, courts are loath to call counterclaims core when they are filed against a proof of claim that was filed "defensively" by a creditor who has already tried to have its claim determined by a court other than the bankruptcy court. *In re Castlerock*, 781 F.2d at 162. This exception does not apply in this case, because Pierce filed his proof of claim offensively.

[21] The Ninth Circuit issued its opinion in *In re Castlerock* soon after the modern bankruptcy code was enacted. In this passage, it also states that "well-settled law" holds "that a creditor consents to jurisdiction over related counterclaims by filing a proof of claim." *In re Castlerock*, 781 F.2d at 162. However, the law it cites in support of this proposition is all pre-*Marathon*, and the court did not specifically consider the impact of *Marathon* on the prior practice of jurisdiction by consent. As indicated, this does not appear to be the law post-*Marathon*. However, the policy reason for the rule could still be the animating force behind § 157(b)(2)(C).

In addition, counterclaims that are permissive, rather than compulsory, do not receive core treatment. A compulsory counterclaim is one that arises out of the same factual transaction as the claim against which it is asserted. Fed.R.Civ.P. 13(a). The bankruptcy court held that Vickie's counterclaim arises out of the same transaction as Pierce's defamation claim. Pierce alleged that Vickie had acted willfully and maliciously by defaming him when her attorneys, at her direction, told members of the press that Pierce used forgery, fraud, and overreaching to gain control of J. Howard, Sr.'s estate. Libel and defamation claims are nondischargeable under § 523(a)(6) when the statements were made with actual knowledge of their falsity. *Wheeler v. Laudani*, 783 F.2d 610, 615 (6th Cir.1986). Thus, at issue, in addition to whether Vickie was responsible for the statements of her attorneys, is whether she knew the statements to be true or false. The bankruptcy court held that proving the truth or falsity of the statements requires proof of some of the same facts as are at issue on Vickie's counterclaim. *Cf. Albright v. Gates*, 362 F.2d 928, 929 (9th Cir.1966) (holding that a counterclaim for recovery of the price paid for oil rights was a compulsory counterclaim to a claim for slander consisting of stating the oil rights were worthless).

However, this nexus between the transactions out of which the claim and counterclaim arise at issue

is somewhat attenuated.[22] Pierce had already obtained a judgment against Vickie's attorneys prior to the time when his claim against Vickie was ruled on by the bankruptcy court. The main issue presented by Pierce's claim is Vickie's responsibility for the statements of her attorneys, not the statements' truth or falsity. Thus, the primary facts at issue on Pierce's claim were the relationship between Vickie and her attorneys and her knowledge or approval of their statements. *See generally In re Durso Supermarkets, Inc.*, 170 B.R. 211, 214 (S.D.N.Y.1994) (holding that when a proof of claim is filed based on a state court judgment, the judgment itself is a different factual transaction from the fact underlying it and thus a counterclaim arising out of the same facts as the underlying action was not core, thereby suggesting that the factual transaction test need not be applied reflexively in all circumstances).

[22] Pierce also argues that even if it arises from the same transaction, Vickie's counterclaim is not compulsory because otherwise-compulsory counterclaims need not be stated if they are the subject of another pending action, and Vickie's counterclaim originally was at issue in the Texas probate proceeding. However, while the party asserting a counterclaim may decline to do so if the counterclaim is the subject of another proceeding, the party is not required to do so. 6 Charles Alan Wright, Arthur R. Miller & Mary Kay Kane, *Federal Practice and Procedure* § 1411, at 87 (3d ed. 1998) ("If defendant elects to interpose the pending claim as a counterclaim, however, he should be allowed to do so, and the counterclaim will be treated as if it were compulsory.").

Thus, it is not certain that Vickie's counterclaim arises from the same transaction as Pierce's proof of claim. Further, considering both the general rule behind the core classification, which stems from the constitutional concerns of *Marathon*, and also the specific policy that underlies § 157(b)(2)(C), the Court concludes that the counterclaim is not core.

As indicated, absent Pierce's filing of a proof of claim regarding the alleged defamation, the counterclaim clearly would be only a non-core, related matter. In this case, the reasons for why counterclaims arising out of the same transaction should usually be considered core do not apply. Counterclaims can be core in essence because of judicial economy and what, as a practical matter, makes good sense for the litigants. The purpose of the rule is to prevent a debtor or trustee from having to split a cause of action by defending against a proof of claim in the bankruptcy proceeding but being unable to assert counterclaims there, instead being forced to pursue counterclaims in a different proceeding or forum. *In re Castlerock*, 781 F.2d at 162. Treating Vickie's counterclaim as core is not necessary to advance these policies in this case.

Here, Vickie's counterclaim dwarfs Pierce's defamation in all respects, both in terms of the time and effort spent litigating it and the size of the potential judgment. On Vickie's motion, the bankruptcy court granted summary judgment to Vickie on Pierce's adversary complaint, holding that Vickie was not responsible for any statements made by her attorneys.

The counterclaim proceeded to trial and has been pending for over two years since then on its own. The bankruptcy court confirmed Vickie's plan of reorganization on March 8, 1999, over six months before the counterclaim went to trial. While arguably the defamation and tortious interference claims arise out of the same factual transaction, this connection is attenuated. Further, the counterclaim raises issues of law entirely different from those raise[d] on the defamation claim.[23]

In *In re Kamine/Besicorp Allegany, L.P.*, 214 B.R. 953, 968-71 (Bankr.D.N.J.1997), the court held that counterclaims asserted by the debtor against a creditor that had filed a proof of claim were not core, notwithstanding the fact that they arose from the same transaction as the proof of claim. The debtor owned and operated a power plant. *Id.* at 955. Prepetition, a dispute arose between it and another entity involved in power production. After the debtor filed for bankruptcy, the other entity filed proofs of claim and then the debtor counterclaimed, asserting in part state common law contract claims. Discussing many of the same arguments advanced by Pierce and Vickie in this case, the court held that the

[23] Considering in particular that the policy underlying the counterclaim rule is that the debtor should not have to split a cause of action into two forums, the Court notes that Vickie in fact voluntarily pursued similar or substantially similar claims in the Texas probate proceeding until after the bankruptcy court entered its final judgment.

counterclaim did not fall within § 157(b)(2)(C) and was not core because the filing of the proof of claim did not "initiate" or "create" the causes of action asserted in the counterclaim. *Id.* at 969. While procedural distinctions render *In re Kamine/Besicorp* not exactly analogous to the present case, this aspect of it is the same: Vickie's counterclaim was not "created" by Pierce's claim. Her dispute with Pierce runs much deeper and broader than his defamation claim and would exist even in the absence of his defamation claim.

In addition, while it does not give it much weight as the issue was not being directly argued, the Court notes that at a hearing in bankruptcy court on July 24, 1996, counsel for Vickie in fact stated that "we believe the counterclaims are related." Pierce's Appendix at 193:22.

Good arguments exist on both sides of this issue, and the Court acknowledges that reasonable jurists might differ in how they would decide it. Formally, Vickie's counterclaim falls within the language of § 157(b)(2)(C) and, barely, it falls within the "same transaction" rule courts have used when applying § 157(b)(2)(C). However, neither of those rules are ends in and of themselves. They serve only as means of amplifying and explicating the distinction drawn in *Marathon*. As the Ninth Circuit stated in *In re Castlerock*, "a court should avoid characterizing a proceeding as 'core' if to do so would raise constitutional problems. The apparent broad reading that can be given to § 157(b)(2) should be tempered by the

Marathon decision." *In re Castlerock*, 781 F.2d at 162; *see also In re Thrall*, 196 B.R. at 968 ("A claim is not core simply because it falls within the wording of § 157(b)(2); the claim must also satisfy the mandate of [*Marathon*]."). When a counterclaim is only somewhat related to the claim against which it is asserted, and when the unique characteristics and context of the counterclaim place it outside of the normal type of set-off or other counterclaims that customarily arise, thus rendering the efficiency concerns not at issue, the counterclaim should not be characterized as core.

IV. CONCLUSION

The bankruptcy court's assertion of federal subject matter jurisdiction over Vickie's counterclaim for tortious interference is AFFIRMED. However, the bankruptcy court's determination that the counterclaim is a core proceeding is REVERSED. Because the counterclaim is a non-core proceeding, the bankruptcy court's judgment is VACATED.

The Court's decision means only that final judgment in this non-core proceeding must be entered by this Court rather than the bankruptcy court. By this order, the Court rules that the bankruptcy court's judgment is proposed rather than final, and therefore neither party has prevailed at the present time. Thus, Vickie's claim against Pierce for tortious interference

has not yet been resolved by any court.[24] This Court will now engage in a comprehensive, complete, and independent review of the bankruptcy court's record and may, if warranted, hear additional testimony from the parties and witnesses. This review will enable this Court to decide whether J. Howard, Sr. promised a gift to Vickie, whether Pierce interfered with that gift, and also whether Pierce has destroyed and failed to produce relevant evidence in a way that justifies the imposition of sanctions.

As a consequence of this ruling, the current arrangements regarding security for a stay on execution of the judgment pending appeal are VACATED.

The Court sets a status conference in this matter for June 4, 2001 at 8:30 a.m. in Santa Ana. Prior to this conference, attorneys for the parties should meet and confer, in person, regarding the effect of this ruling on all matters pending between these and related parties. They shall file a joint status report regarding such issues no later than May 31, 2001 at 4:00 p.m.

Because this order involves two "controlling question[s] of law as to which there is substantial ground for difference of opinion and . . . an immediate appeal from the order may materially advance the ultimate termination of the litigation," 28 U.S.C. § 1292(b), the Court hereby CERTIFIES this order for interlocutory

[24] Vickie's claim against Pierce individually was not addressed or determined by the Texas probate court.

appeal as to both the issue of the probate exception and the issue of whether Vickie's counterclaim is a core or non-core proceeding. Any appeal from this order shall not stay proceedings before this Court unless the Court of Appeals so orders.[25]

IT IS SO ORDERED.

[25] The Court originally issued this order on May 24, 2001, without including any statement as to certification under 28 U.S.C. § 1292(b). Because a § 1292(b) certification must be in the order certified for appeal itself, the Court now issues this order in amended form including the requisite statement. *See* 28 U.S.C. § 1292(b) and Fed. R.App. P. 5(a)(3).

257 B.R. 35

United States Bankruptcy Court,
C.D. California.
In re Vicki Lynn MARSHALL, Debtor.
E. Pierce Marshall, Plaintiff,
v.
Vicki Lynn Marshall, Defendant.
Vicki Lynn Marshall, Counterclaimant,
v.
E. Pierce Marshall, Counterdefendant.
Bankruptcy No. LA 96-12510-SB.
Adversary No. 96-01838-SB.

Dec. 29, 2000.

John P. Melko, Verner, Liipfert, Bernhard, McPherson and Hand, Chartered, Houston, TX.

Joseph A. Eisenberg P.C., Jeffer, Mangels, Butler & Marmaro LLP, Los Angeles, CA.

Philip W. Boesch, Jr., Gregory J. Aldisert, Joshua A. Meyer, Kinsella, Boesch, Fujikawa & Towle, LLP, Los Angeles, CA.

Rex S. Heinke, Greines, Martin, Stein & Richard LLP, Beverly Hills, CA.

ORDER ON MOTION FOR ENTRY OF JUDGMENT

SAMUEL L. BUFFORD, Bankruptcy Judge.

Trial in this adversary proceeding took place in October and November, 1999. It has come time to resolve the remaining issues in this adversary proceeding, and to issue a judgment. This opinion

addresses three issues: (1) whether the alleged probate exception to federal jurisdiction applies to this adversary proceeding; (2) whether this is a "core proceeding" within the meaning of 28 U.S.C. § 157(b); and (3) what form the judgment in this adversary proceeding should take.

A. Jurisdiction

E. Pierce Marshall continues to complain that this court lacks jurisdiction over this adversary proceeding because this claim belongs in the probate case now in trial in Texas. Notably, however, he has never brought a motion on this subject on proper notice pursuant to this court's motion rules. For this reason alone this issue has never been properly brought before this court, and E. Pierce Marshall is entitled to no relief on this subject.

In addition, by filing his claim in this bankruptcy case and by filing this adversary proceeding against Vicki Marshall, E. Pierce Marshall voluntarily submitted to the jurisdiction of this bankruptcy court.

He cannot now complain of the consequences thereof, especially after the court has ruled on the merits of his dispute with Vicki Marshall.

1. Supreme Court Case Law

The extent of the equity jurisdiction of the bankruptcy court in this case is governed by United States Supreme Court precedent. The Supreme Court has

stated, "by filing a claim against a bankruptcy estate the creditor triggers the process of allowance and disallowance of claims, thereby subjecting himself to the bankruptcy court's equitable power." *Langenkamp v. Culp,* 498 U.S. 42, 44, 111 S.Ct. 330, 331, 112 L.Ed.2d 343 (1990) (internal quotes omitted).

This equity jurisdiction of the bankruptcy court includes both claims *by* the creditor against the estate and claims *against* the creditor by the estate's representative. In *Langenkamp,* for example, the Supreme Court found that a preference action filed against a creditor who had filed a claim was "a part of the claims-allowance process," and that the filing of the claim waived the right to a jury trial in the preferential transfer adversary proceeding. *Id.* "In other words," the Supreme Court said, "the creditor's claim and the ensuing preference action by the trustee become integral to the restructuring of the debtor-creditor relationship through the bankruptcy court's equity jurisdiction." *Id.*

By contrast, in an earlier case the Supreme Court found that a fraudulent transfer adversary proceeding did not come within the "process of allowance and disallowance of claims." *Granfinanciera, S.A. v. Nordberg,* 492 U.S. 33, 57-59, 109 S.Ct. 2782, 2799, 106 L.Ed.2d 26 (1989) (holding that defendants had a right to a jury trial). The Supreme Court reached this result, however, only because the defendants had *not* filed claims in the bankruptcy case. *See Langenkamp,* 498 U.S. at 44-45, 111 S.Ct. at 331. Indeed, the purpose of *Langenkamp* was to eliminate

any speculation that the right to a jury trial might survive the filing of a claim in the bankruptcy case, and to make clear that the equity jurisdiction of the bankruptcy court extended to all claims between a creditor and the estate, once the creditor files a claim.

Similarly, in *Hong Kong & Shanghai Banking Corp. v. Simon (In re Simon)*, 153 F.3d 991 (9th Cir.1998), the Ninth Circuit found that, by filing a claim, the bank "forfeited any right it had to claim that the court lacked the power to enjoin [it] from commencing a post-bankruptcy collection proceeding against the debtor" in Hong Kong. *Id.* at 997.

The teaching of *Langenkamp, Granfinanciera* and *Simon* is that the filing of a claim in a bankruptcy case has substantial procedural consequences for the claimant. By filing a claim, a claimant voluntarily submits to the equity jurisdiction of the bankruptcy court for the allowance and disallowance of all claims made *by* the claimant against the bankruptcy estate or made *against* the claimant by the bankruptcy estate's representative.

E. Pierce Marshall filed his claim against the bankruptcy estate in this case. He thus voluntarily submitted himself to the bankruptcy court's equity jurisdiction as to all claims by the estate against him, including the claims asserted in this adversary proceeding.

2. The "Probate Exception" to Federal Jurisdiction

E. Pierce Marshall also argues that this court has no jurisdiction over debtor's counterclaim because it essentially involves a probate matter pending in a Texas court that is subject to a probate exception to federal jurisdiction.

While there is a probate exception to federal jurisdiction, it is applicable principally to diversity jurisdiction under 28 U.S.C. § 1332 (2000). *See, e.g., Georges v. Glick,* 856 F.2d 971 (7th Cir.1988) (holding that probate exception applies only in diversity cases); *Goerg v. Parungao* (*In re Goerg*), 844 F.2d 1562 (11th Cir.1988) (same).[1] As the court in *Goerg* specifically stated, "[t]hat exception relates only to 28 U.S.C. § 1332 (1982), and has no bearing on federal question jurisdiction, the jurisdiction invoked in bankruptcy cases." *Id.* at 1565 (footnote omitted). The court in *Goerg* further warned: "[c]are should be taken not to confuse the question of the breadth of Congress' bankruptcy power with the so-called "probate exception" to statutory diversity jurisdiction." *Id.* Furthermore, the probate exception to diversity jurisdiction must be narrowly construed. *Georges,* 856 F.2d at 973. The court in *Goerg* declared generally: "[o]wing to the supremacy clause, federal bankruptcy law preempts state law; as one of Congress' enumerated powers, the

[1] Notably, E. Pierce Marshall fails to cite either of these cases.

power to enact bankruptcy laws is limited only by the substantive guarantees contained in the Constitution." *Goerg*, 844 F.2d at 1565.

Virtually all of the cases that E. Pierce Marshall cites in support of his argument are diversity cases, and thus are inapplicable in this case. As in the *Goerg* case, this court's jurisdiction over this adversary proceeding rests on the federal question jurisdiction applicable in bankruptcy cases.

Goerg and *Georges* may overstate the lack of a probate exception to federal jurisdiction. In *Markham v. Allen*, 326 U.S. 490, 66 S.Ct. 296, 90 L.Ed. 256 (1946)[2], the Supreme Court held that a federal court may properly exercise jurisdiction over a case brought against the executor and resident heirs of a decedent's estate that was in the course of probate administration in state court. Federal jurisdiction arose under the Trading With the Enemy Act, where the plaintiff was a federal officer authorized to receive inheritances in place of German heirs during World War II.

[2] E. Pierce Marshall also relies on two quite old United States Supreme Court decisions, which the court finds inapposite. In *Sutton v. English*, 246 U.S. 199, 38 S.Ct. 254, 62 L.Ed. 664 (1918), a suit to annul a will, the Supreme Court found no federal question and no diversity of citizenship, and thus no colorable basis for federal jurisdiction. *Id.* at 200, 208, 38 S.Ct. 254. In *O'Callaghan v. O'Brien*, 199 U.S. 89, 25 S.Ct. 727, 50 L.Ed. 101 (1905), the Supreme Court found that the only asserted ground for federal jurisdiction was frivolous. *Id.* at 100-01, 25 S.Ct. 727.

The Supreme Court in *Markham* found that the probate limitation on federal jurisdiction only prohibits a federal court from probating a will, administering a decedent's estate, or assuming control of property in the custody of the state court. *See id.* at 494, 66 S.Ct. 296. The Supreme Court found that a federal court may properly adjudicate rights in probate property, so long as its final judgment does not undertake to interfere with the state court's possession of the property. *Id.* The Supreme Court held that the lower court's ruling that the plaintiff was entitled to all of the net probate estate after payment of debts, taxes and expenses of administration was a proper exercise of federal jurisdiction. *Id.* at 495, 66 S.Ct. 296.

The *Markham* rationale would permit this court to determine (if appropriate on the merits) that Vicki Marshall is entitled to all (or a portion) of the net assets in the possession of the Texas probate court (except as to any parties over whom this court has not had jurisdiction). However, this court's rulings do not affect the disposition of the Texas probate assets.

E. Pierce Marshall relies particularly on *Beren v. Ropfogel,* 24 F.3d 1226 (10th Cir.1994), which involved a claim for an expectation of inter vivos gifts or testamentary dispositions. This case, which also appears to be a diversity case, provides no assistance to E. Pierce Marshall. The court sustained the dismissal of claim for an expectation of a gift or testamentary devise on the grounds of failure to state a

claim for relief, not on jurisdictional grounds. *See id.* at 1229-30.

Furthermore, the "probate exception" issue has never been properly brought before this court. This issue was first raised by Pierce Marshall in a motion *in limine* that was filed on October 18, 1999, and set for hearing on the first day of trial on October 28, 1999. This procedure violated the court's motion rule, Local Rule 9013-1, which requires 21 days notice of a motion (24 days if served by mail). The court finds that this issue was raised at that time principally for the purpose of delaying the trial.

Pierce Marshall waived his right to make this argument by waiting until several rounds of sanctions had been imposed on him before raising it. Ninth Circuit law holds that a party cannot wait until trial, after the case is going badly for that party, to raise a jurisdictional issue. *See Hill v. Blind Industries & Services,* 179 F.3d 754 (9th Cir.1999).

The court finds that the "probate exception" argument was waived because it was not raised in a timely fashion. A renewal of this argument now, a year after trial, at the time for entry of judgment, is likewise not timely.

3. Abstention

On January 6, 1997 E. Pierce Marshall filed his motion contending that mandatory or discretionary abstention applied to Vicki Marshall's counterclaim.

As to mandatory abstention, E. Pierce Marshall argued that this portion of the dispute should be heard in a court in Louisiana rather than this court, because J. Howard Marshall II's probate case was pending there. In fact, shortly thereafter the Louisiana Supreme Court dismissed the probate action for lack of jurisdiction. Probate proceedings were subsequently filed in Harris County Court in Houston Texas, and remain pending.

E. Pierce Marshall's motion for abstention was untimely. It was not even filed until eight months after this adversary proceeding was filed, at which time this adversary proceeding was well under way.

This court's denial of mandatory abstention has been vindicated both by the lack of Louisiana jurisdiction all together, and by the fact that the trial in the Texas probate action did not begin until nearly four years after this court denied E. Pierce Marshall's motion for abstention, and nearly a year after this court's own trial in this adversary proceeding, and still remains pending.

This court ruled on the abstention motion in 1997, and this ruling is now only subject to review on appeal.

B. Counterclaim as a Core Proceeding

On July 8, 1996 E. Pierce Marshall moved for dismissal of the counterclaim on the grounds of lack of jurisdiction. In opposition to the motion to dismiss,

Vicki Marshall asserted that the counterclaim fell within this court's core jurisdiction under 28 U.S.C. § 157(b)(2)(C), on the grounds that the counterclaim in the adversary proceeding was in substance a counterclaim against E. Pierce Marshall's claim against the estate.

At the hearing on August 14, 1996 the court found that the counterclaim in the adversary proceeding was in substance also a counterclaim to Pierce Marshall's claim filed in this case, pursuant to which he voluntarily submitted to the jurisdiction of this court. The court found that the only substantial difference between E. Pierce Marshall's claim that he filed in the bankruptcy case and the complaint that he filed in the adversary proceeding was that in the adversary proceeding he sought a determination that the debt asserted in the claim was nondischargeable. The court further found that the counterclaim arose out of the same transactions and occurrences as the claim and the adversary complaint. Because of the close relation between E. Pierce Marshall's claim and his adversary complaint, the court consolidated the proceedings for all purposes, including trial and judgment.

E. Pierce Marshall raised a question at oral argument whether *Piombo Corp. v. Castlerock Properties* (*In re Castlerock Properties*), 781 F.2d 159 (9th Cir.1986), would require a finding that the counterclaim is not a core proceeding. *Castlerock* is clearly a different case from this. In *Castlerock* the Ninth Circuit found that adversary proceeding at issue was not

a core proceeding, because it was filed before the creditor filed its claim in the bankruptcy case. *Id.* at 161-62. Here, to the contrary, the counterclaim was filed in the adversary proceeding voluntarily filed by E. Pierce Marshall in this court, after he had also voluntarily filed his claim in this case. His voluntary submission to the jurisdiction of this court could not be more clear.

Furthermore, the court's August 14, 1996 determination that the counterclaim and the adversary proceeding was also essentially a counterclaim to Pierce Marshall's claim is not now open to further consideration in this court, unless an appellate court should require such further consideration.

Because this is a core proceeding, the court has power to enter judgment. As to related proceedings only, the court prepares findings of fact and conclusions of law and recommend a judgment, which is submitted to the district court for *de novo* review. *See* 28 U.S.C. § 157(c)(1). However, for a core proceeding the bankruptcy court enters its own judgment.

C. Entry of Judgment

Vicki Marshall has moved this court for entry of judgment on her counterclaim now, rather than delay until the completion of the probate trial in Texas. E. Pierce Marshall opposes the entry of judgment at the present time. The court finds the arguments of Vicki Marshall well taken, and the arguments of E. Pierce Marshall unpersuasive.

In the Court's order of October 6, 2000 the court determined that entry of judgment should await the resolution of the probate action in Texas, on the grounds that a calculation of Vicki Marshall's damages cannot be made until the probate court determines what inheritance Vicki Marshall is entitled to receive from her deceased husband J. Howard Marshall II. The court determined that Vicki Marshall's damages (excluding punitive damages, subsequently awarded in the amount of $25 million) amounted to $449,754,134, less whatever she recovers in the probate action. Upon further consideration, and evaluation of the arguments of the parties, the court is persuaded that judgment can be awarded at the present time in a form to take account of any recovery by Vicki Marshall in the Texas probate action. Such a recovery is accommodated as follows: any amount that Vicki Marshall recovers in the probate action will count as partial (or full) satisfaction of the judgment issued herein.

The court finds a further reason for issuing judgment in this adversary proceeding sooner rather than later. E. Pierce Marshall appears to be planning to take an appeal in this dispute, and has made a motion for leave to file an interlocutory appeal. The sooner this court issues its judgment, the sooner a definitive appellate process can begin.

D. Injunctive Relief

In addition to a money judgment, the debtor requests injunctive relief as a part of this court's judgment. A claim for such relief is contained in the counterclaim. No preliminary injunctive relief was sought in this adversary proceeding. Thus the issue is limited to the issuance of a permanent injunction as part of this court's judgment.

Injunctive relief is not normally available as part of a money judgment. Rule 69 of the Federal Rules of Civil Procedure, incorporated by reference in Rule 7069 of the Federal Rules of Bankruptcy Procedure, incorporates by reference the state law for enforcement of judgments. Vicki Marshall has not shown that injunctive relief is also available as part of a judgment.

The United States Supreme Court touched on this issue in *Grupo Mexicano v. Alliance Bond Fund, Inc.*, 527 U.S. 308, 119 S.Ct. 1961, 144 L.Ed.2d 319 (1999), where it found that a federal court may not issue a preliminary injunction to restrain lawful conduct to protect an anticipated judgment of the court. The Supreme Court observed that the equitable action known as a "creditors bill" is traditionally available to permit a judgment creditor to discover the debtor's assets, to reach equitable interest not subject to execution at law, and to set aside fraudulent conveyances. *See id.* at 319, 119 S.Ct. 1961. The Court noted that, as a general rule, a creditors bill could be brought only by a creditor who had already

obtained a judgment establishing the debt. *Id.* The Court further noted that the law of fraudulent conveyances in bankruptcy was developed to prevent the hiding of assets by a defendant while litigation was in process. The Court also noted that state statutes eliminating the need for a judgment before bringing a fraudulent conveyance claim may have altered the common law rule and may permit the tying up of a defendant's assets while litigation is pending. *See id.*, at 324 n. 7, 119 S.Ct. 1961.

This court finds that the debtor has not shown her entitlement to injunctive relief in support of her money judgment. Accordingly, injunctive relief is denied at this point. However, the denial of injunctive relief is without prejudice to bringing in appropriate judgment enforcement procedures.

By separate document the court is issuing a judgment consistent with its rulings herein and in its prior orders.

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Attorneys for Debtor and Counterclaimant
VICKIE LYNN MARSHALL

UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA
LOS ANGELES DIVISION

In re VICKIE LYNN MARSHALL, Debtor. E. Pierce Marshall, Plaintiff, vs. Vickie Lynn Marshall, Defendant.	) BANKR. CASE NO. LA 96-12510SB) Adversary No. 96-01838)) Bankr Judge: Hon. Samuel L. Bufford) **FINAL JUDGMENT**) (Filed Dec. 29, 2000))) TRIAL DATE: October 25, 1999) DATE: December 6, 2000

Vickie Lynn Marshall, Counterclaimant, vs. E. Pierce Marshall, Counterdefendant.	)	TIME: 11:00 PLACE: Courtroom 1575 Roybal Federal Building 255 E. Temple Street Los Angeles, CA 90012

TO THE HONORABLE SAMUEL L. BUFFORD, UNITED STATES BANKRUPTCY JUDGE, AND OTHER INTERESTED PARTIES:

This action came on for trial before the Court, and the issues having been duly tried and a decision having been duly rendered,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED that judgment be entered in favor of Vickie Lynn Marshall, and against E. Pierce Marshall, as follows:

1. That Vickie Lynn Marshall recovers from E. Pierce Marshall compensatory damages in the amount of $449,754,134.

2. That the above amount shall bear interest from and including October 6, 2000 at the rate set forth in 28 U.S.C. § 1961.

3. That Vickie Lynn Marshall recovers from E. Pierce Marshall punitive damages in the amount of $25,000,000.

4. That the above amount shall bear interest from and including November 21, 2000 at the rate set forth in 28 U.S.C. § 1961.

5. That E. Pierce Marshall recovers nothing against Vickie Lynn Marshall.

6. That Vickie Lynn Marshall recovers from E. Pierce Marshall her costs of suit in this entire action in the amount of .

7. That the amounts, if any, which are hereinafter collected for release or satisfaction of claims made in the Texas probate action shall be deemed to be payments made toward satisfaction of this judgment.

8. That E. Pierce Marshall, his agents, employees, representatives and all persons acting in concert or participating with him, are directed to endorse and deposit with the Clerk of this Court, or anyone the Court appoints for this purpose, 4,283,325 shares of Koch Industries, Inc. ("Koch") common stock and 1934 shares of Koch preferred stock, which constitute 50% of the Koch shares held by E. Pierce Marshall individually or through Marshall Petroleum, Inc. ("MPI"), Trof, Inc., or its successors or assigns or the proportionate number of Koch shares in the event that Koch issues additional shares (e.g. stock split) which will be held until such time as the money judgment set forth above has been satisfied. Notwithstanding the above, all or part of such stock may be released in response to a writ of execution on the money judgment set forth above. [/s/ SLB]

9. That E. Pierce Marshall, his agents, employees, representatives and all persons acting in concert or participating with him, are enjoined and restrained (except or as provided in paragraph 7 above or in connection with a writ of execution on this money judgment) from directly or indirectly transferring, encumbering, or otherwise restricting or alienating, by any means whatsoever, E. Pierce Marshall's interest in Koch, whether held by E. Pierce Marshall individually or through MPI, Trof, Inc., or its successors or assigns, until such time as the money judgment set forth above has been satisfied. [/s/ SLB]

10. That E. Pierce Marshall, his agents, employees, representatives and all persons acting in concert or participating with him, shall pay to Debtor any and all proceeds or dividends from said Koch stock whether held by E. Pierce Marshall individually or through MPI, Trof, Inc. or its successors or assigns, into an interest-bearing trust account for the sole benefit of Vickie Lynn Marshall from the date of this judgment until such time as the money judgment set forth above has been satisfied, withdrawals from which may only be made for the purpose of satisfying the money judgment set forth above or in connection with a writ of execution on this Judgment. [/s/ SLB]

11. The Court shall retain jurisdiction of this case for such other and further orders as may be necessary. [/s/ SLB]

DATED: 12/29/2000

/s/ Samuel L. Bufford
HONORABLE
SAMUEL L. BUFFORD
UNITED STATES
BANKRUPTCY JUDGE

UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA

In re VICKIE LYNN MARSHALL, Debtor. E. Pierce Marshall, Plaintiff, vs. Vickie Lynn Marshall, Defendant. Vickie Lynn Marshall, Counterclaimant, vs. E. Pierce Marshall, Counterdefendant.	Case No. LA 96-12510-SB Adv. No.: LA 96-01838-SB Chapter 11 **SUPPLEMENTAL MEMORANDUM OF DECISION FOLLOWING TRIAL** (Filed Nov. 21, 2000) DATE: December 6, 2000 TIME: 11:00 a.m. CTRM: 1575

The court on its own motion hereby supplements its amended decision of October 6, 2000 to clarify the court's ruling that this is a core proceeding, to issue its ruling on punitive damages, and to set a further hearing on the proposed findings of fact, conclusions of law and form of judgment to be entered in this adversary proceeding.

1. Core Proceeding

This proceeding began as a proof of claim for defamation that E. Pierce Marshall filed in this chapter 11 case pursuant to Bankruptcy Code § 501. In response to Pierce Marshall's proof of claim, the debtor objected to the claim and filed a counterclaim for tortious interference with her expectancy of a gift from her deceased husband J. Howard Marshall II, who was Pierce Marshall's father. The counterclaim turned the claim objection into an adversary proceeding pursuant to Rule 3007 of the Federal Rules of Bankruptcy Procedure.

On summary judgment, the debtor prevailed on Pierce Marshall's claim. The debtor also prevailed on the counterclaim after trial on the merits in November, 1999. *See Marshall v. Marshall* (*In re Marshall*), 253 B.R. 550 (Bankr. C.D. Cal. 2000).

The court has previously determined that this adversary proceeding is a core proceeding, as defined in 28 U.S.C. § 157. Section 157(b)(2) provides in relevant part:

> Core proceedings include . . .
>
> . . .
>
> (B) allowance or disallowance of claims against the estate . . . ;
>
> (C) counterclaims by the estate against persons filing claims against the estate. . . .

28 U.S.C. § 157 (West 2000). Both the objection to claim and the counterclaim are thus core proceedings under this statutory definition. *See Sun West Distribs., Inc. v. Grumman Energy Sys. Co. (In re Sun West Distribs., Inc.)*, 69 B.R. 861, 864 (Bankr. S.D. Cal. 1987).

2. Punitive Damages

The court has previously determined that this is a proper case for the award of punitive damages. After further examination of the record in this case, the court concludes that the time is now ripe to award the punitive damages.

The major purpose of awarding punitive damages is to punish and deter the wrongful conduct of a party. Under Texas law, the courts generally consider five factors in determining a reasonable punitive damages award: (1) the nature of the wrong; (2) the character of the conduct involved; (3) the degree of culpability of the wrongdoer; (4) the situation and sensibilities of the parties concerned; and (5) the extent to which the defendant's conduct offends the public sense of justice and propriety. *See, e.g., Alamo Nat'l Bank v. Kraus*, 616 S.W.2d 908, 910 (Tex. 1981); *North Am. Refractory Co. v. Easter*, 988 S.W.2d 904, 920 (Tex. App. 1999); *Cantu v. Burton*, 921 S.W.2d 344, 351 (Tex. App. 1996). The amount of punitive damages to award the debtor requires the court to evaluate the actions of Pierce Marshall in light of these five factors.

In its prior ruling the court has made findings on two of these factors: the nature of the wrong and the character of the conduct involved. Three factors remain to be examined: the degree of Pierce Marshall's culpability, the extent to which his conduct offends the public sense of justice and propriety, and the situation and sensibilities of the parties. In addition, certain of the court's findings in *Marshall, supra*, are pertinent to all of these factors, and are incorporated herein by reference.

a. Degree of Culpability

In determining the degree of culpability under Texas law, the court considers the defendant's state of mind, the degree of his or her conscious indifference, and his malice. *See Ellis County State Bank v. Keever*, 936 S.W.2d 683, 687 (Tex. 1996). Texas law defines malice as ill will, evil motive, gross indifference or reckless disregard of the rights of others, which may be established by direct or circumstantial evidence. *See J.C. Penny Company, Inc. v. Ruth*, 982 S.W.2d 586, 590 (Tex. 1998).

The court finds that Pierce Marshall's actions as previously determined were undertaken with intentional disregard for the rights of the debtor and the procedures of this court. The court finds that Pierce Marshall's behavior towards the debtor is intentional and reprehensible, and that it constitutes malice toward her.

b. Situation and Sensibilities of the Parties

The situation and sensibilities of the parties refers to evidence of remorse, remedial measures, and ability to pay punitive damages. *See Keever*, 936 S.W.2d at 688.

Pierce Marshall has shown no remorse whatsoever with regard to his tortious actions to keep the debtor from receiving the share of her husband's fortune that he directed his lawyers to arrange for her. Moreover, Pierce Marshall has continued to disobey the court's orders to produce documents for discovery and has raised objections that the court has repeatedly found to be frivolous.

The wealth of the defendant is relevant in determining the amount of punitive damages because such information assists the court in determining an amount sufficient to effectively punish the defendant *See White v. Sullins*, 917 S.W.2d 158, 163 (Tex. 1996). Pierce Marshall has obtained for himself and his immediate family the entire 16% interest in Koch Industries that his father held. This court has found that these assets were worth more than $1.6 billion as of August 31, 1999. The court finds that Pierce Marshall easily has the ability to pay the punitive damages assessed herein.

d. Offending Public Sense of Justice and Propriety

Finally, the Court believes that Pierce Marshall's actions described in this court's prior ruling offend the public sense of justice and propriety. In particular, his totally unjustified refusal to provide discovery in this adversary proceeding has prevented this court from determining this adversary proceeding on its merits. Because this is a high profile case that has attracted substantial public attention, Pierce Marshall's conduct substantially promotes a disrespect for the federal courts and the degree of justice that they dispense.

At the same time, the court must keep its mind that an award of punitive damages is subject to due process considerations prohibiting grossly excessive punishment. *See BMW v. Gore*, 517 U.S. 559 (1996).

In light of all these factors, the court assesses punitive damages against Pierce Marshall in the amount of $25 million. In the court's judgment, this amount sufficiently serves the purpose of punishing and deterring Pierce Marshall's behavior. At the same time, the amount of the damages satisfies constitutional considerations regarding excessiveness.

3. Findings of Fact and Conclusions of Law

The debtor requests that the court enter certain specified additional findings of fact and conclusions of law not incorporated into its amended *Marshall*

decision. *See* Emergency Ex Parte Application for Entry of Final Judgment and for Entry of Supplemental Findings, at 9. Requests 2 and 3 are denied. Pierce Marshall is hereby given an opportunity to respond to Requests 1 and 4 by November 30, 2000. A hearing on these requests is set for December 6, 2000 at 11:00 a.m.

4. Nature and Form of Judgment

Because the court has now made its award of punitive damages, judgment is now ready for entry in this adversary proceeding. Such a judgment should include the award of $449,754,934 in compensatory damages and $25 million in punitive damages.

The debtor also requests an injunction against Pierce Marshall, to require him (1) to deposit 428,333 shares of common stock in Koch Industries, Inc. and 1934 shares of preferred stock with the court; (2) to prohibit Pierce Marshall and his agents from transferring or encumbering these shares of Koch stock; and (3) to require that all dividends on these shares of stock be deposited into a trust account for the debtor. These provisions would remain in force until this court's money judgment is satisfied.

The court questions whether these provisions are appropriate as a part of the court's judgment. The court particularly would like to see authority that such an order is appropriate in place of enforcement procedures to be undertaken by the debtor.

The court directs the parties to brief this issue for the December 6 hearing. Any briefs by the debtor in support of these provisions shall be served by same day delivery and filed by November 28, 2000. Any opposition shall be served by same day delivery and filed (with a copy delivered to chambers) by December 1, 2000.

Dated: November 21, 2000

/s/ Samuel L. Bufford
Samuel L. Bufford
United States
Bankruptcy Judge

[Certificate Of Mailing Omitted In Printing]

253 B.R. 550

United States Bankruptcy Court, C.D. California.
In re Vickie Lynn MARSHALL, Debtor.
E. Pierce Marshall, Plaintiff,
v.
Vickie Lynn Marshall, Defendant.
Vickie Lynn Marshall, Counterclaimant,
v.
E. Pierce Marshall, Counterdefendant.
Nos. LA 96-12510-SB, LA 96-01838-SB.

Oct. 6, 2000.

AMENDED MEMORANDUM OF DECISION FOLLOWING TRIAL

SAMUEL L. BUFFORD, Bankruptcy Judge.

I. Introduction

Debtor Vicki Lynn Marshall, also known as Anna Nicole Smith, is the surviving widow of J. Howard Marshall II, who was said to be the richest man in Texas.[1] Nonetheless, E. Pierce Marshall, J. Howard's[2] second son from a prior marriage, contends in the probate case now in trial in Probate Court in Houston, Texas that J. Howard died essentially

[1] Testimony in a prior trial in an adversary proceeding in this bankruptcy case indicates that there may have been one Texan more wealthy than J. Howard at the time of his death.

[2] Because all of the principals in this case have the same last name, the court will refer to them by their first or second names, according to how they are commonly known.

penniless. In this adversary proceeding the court finds that Pierce tortiously interfered with Vickie's expectancy of an *inter vivos* gift that J. Howard instructed his attorneys to arrange.

The court finds that Vickie has suffered damages in the amount of $449,754,134, less whatever she receives from the probate of J. Howard's estate. These damages are mainly based on sanctions imposed on Pierce for his egregious discovery abuse in this adversary proceeding. A final calculation of the damages remains to be determined upon the completion of the probate case.

II. Findings of Fact

This adversary proceeding came on for trial on October 27, 1999 and proceeded for five days over a period of a week and a half. The court has heard the testimony of the witnesses who testified at trial, considered the testimony of those that appeared through deposition transcript, and evaluated the credibility of all of the witnesses. Insofar as the testimony of any witness conflicts with the findings herein (including findings imposed as discovery sanctions), the court finds that such testimony is not credible.

Vickie filed this bankruptcy case on January 25, 1996, a few months after the decease of her husband J. Howard. His estate remains tied up in a probate proceeding in Texas, where a trial is now in process. It appears that Vickie filed this bankruptcy case for two reasons: she had just suffered an $884,607.98

default judgment to her housekeeper Maria Cerrato on sexual misconduct claims,[3] and she had not received any inheritance from J. Howard.

Under her professional name of Anna Nicole Smith, Vickie has pursued an acting and modeling career. She appeared on the cover photo of Playboy Magazine in March, 1992, as the centerfold Playmate of the month in the May, 1992 issue, and as the Playmate of the Year for 1992. She is also known for her television appearances as a model for Guess Jeans. J. Howard promoted and encouraged this career before and during their marriage and paid for acting lessons for her.

After a courtship that lasted some two and a half years, Vickie agreed to marry J. Howard in June, 1994, and they were married immediately. At that time J. Howard was 89 years old, and Vickie was 26. This was the third marriage for J. Howard, and the second for Vickie. J. Howard had two sons from his first marriage, J. Howard Marshall III and Pierce. Vickie had a son from her prior marriage. While a prenuptial agreement was drafted, it was never signed by the parties.

J. Howard's wealth consisted principally in his ownership of approximately 16% of the outstanding shares of stock in Koch Industries, Inc. [hereinafter KII], the second largest privately held corporation in

[3] The sexual harassment case was subsequently settled.

the United States. The Marshall interest in the KII stock was held by Marshall Petroleum, Inc. [hereinafter MPI]. J. Howard's interest in MPI was 70.51776%. The 16% interest in KII is particularly valuable because it was the controlling interest in deciding a family dispute in the early 1980's between two factions of the Koch family.[4] Most of the income of KII has been reinvested in the business: typically less than ten percent has been distributed to shareholders.

As an inducement to marry him, J. Howard promised Vickie that he would leave her half of what he had. J. Howard made this promise repeatedly, both before and after the marriage.

In December, 1992 J. Howard instructed Harvey Sorensen, an attorney who represented him from time to time, to arrange a gift to Vickie, "his future wife," of a half interest in his "new community." This gift was to be structured so that the value of the gift was to be measured by J. Howard's interest in the increase in value of the underlying KII stock held by MPI. A few days earlier J. Howard also instructed Jeff Townsend, another attorney who did work for J. Howard, to arrange for Edwin Hunter, a third attorney, to prepare a "catch-all trust" for Vickie's benefit.

[4] After the dust settled in 1981, Charles Kock and David Kock each held 40-41% of the KII stock, J. Howard held 16%, and the remainder was held by employees pursuant to an employee stock option plan.

Neither of these projects was completed **because Pierce fired Sorensen and conspired with Hunter to prevent the drafting and execution of the documents that would have accomplished the gift that J. Howard had directed.**[5]

At the time of trial,[6] J. Howard's interest in the KII stock was worth $1,640,978,961.[7] From the time that J. Howard and Vickie were married to the date of trial, the value of the stock increased by $449,754,134.

In 1982 J. Howard set up a Living Trust to hold his assets,[8] and eventually transferred the MPI stock into the Trust. J. Howard was the trustee. At the time of Vickie's marriage to J. Howard, Pierce and his family were the sole beneficiaries of the trust: neither Vickie nor J. Howard Marshall III had any beneficial interest in its assets. However, J. Howard had the power to revoke the Trust at any time, in which event the trust assets would revert to J. Howard.

[5] The text in bold print consists in findings that the court makes as sanctions for the discovery violations that are discussed *infra*.

[6] The actual valuation date for the KII stock for the purposes of trial was August 31, 1999.

[7] The court assumes that the KII stock is now worth more than $2 billion because the price of oil has increased more than 50% in the last year.

[8] Exhibit A to the trust instrument is supposed to be a list of assets transferred into the trust. This exhibit has apparently never been produced in this adversary proceeding.

For many years Pierce was fearful that his father J. Howard would give away a substantial part of the wealth that Pierce wanted to inherit. Pierce often argued with J. Howard about money and about J. Howard's gifts to Vickie. Pierce also resented the gifts that J. Howard gave to Lady Walker, his mistress who had died shortly before J. Howard met Vickie, and Pierce brought aggressive litigation against Lady Walker's heirs to challenge their right to what he considered Marshall property. J. Howard did not care about Pierce's views on these subjects.

As soon as Pierce learned of his father's marriage to Vickie, he contacted attorney Edwin Hunter, to take action to assure that Vickie did not receive any of the assets in the Living Trust. Pierce was concerned because his father had been especially generous to Lady Walker, his father's mistress for many years who had died in 1990, and he feared that his father would be equally generous to Vickie. In response, Hunter devised a plan to make the trust irrevocable, so that the assets would be protected for Pierce and his family.

The next week Pierce and Hunter met with J. Howard to review a document entitled, "J. Howard Marshall, II Post Nuptial Fine Tuning of Estate Plan" [hereinafter the Fine Tuning Document]. This document contained proposed amendments to the Living Trust.

J. Howard relied on Pierce and Hunter to inform him of the contents of the document. By that time J. Howard's eyesight had deteriorated to the point where he was not able to read any text finer than a newspaper headline.[9] Apparently, J. Howard signed[10] the Fine Tuning Document.[11]

However, the change that made the Living Trust irrevocable was not in the Fine Tuning Document at the time that J. Howard apparently signed it.[12] **Pierce caused this change to be added to page two of the Document at a later date, likely after J. Howard's death.**[13]

[9] However, J. Howard's mental capacities remained intact until his death.

[10] The records of Eyvonne Scurlock, the notary who allegedly notarized J. Howard's signature on the Fine Tuning Document, are in shambles and have no credibility. Among other defects, items are out of sequence, key pages are torn out, blank pages are interspersed between those containing notarial records, and she notarized signatures that she did not witness. Indeed, for the first ten years she served as a notary she kept no notarial records at all and did not know that they were required.

[11] The court is informed that the authenticity of J. Howard's signature on the trust amendment is at issue in the Texas Probate Court. This issue is left for decision by that court.

[12] In addition to what the court finds based on the evidence, the findings in this sentence are also adopted as sanctions for Pierce's discovery violations, as discussed *infra*.

[13] After trial, Vickie moved to reopen the record to submit the testimony of Donald J. Fandry, an expert who examined the Fine Tuning Document. The second page of the Document, which contains the provision making the trust irrevocable, is very different from the remaining pages of the document in the

(Continued on following page)

After his father's death, Pierce has continued his plot to prevent Vickie from obtaining any Marshall family assets. Pierce contends that essentially all of J. Howard's assets were in the Living Trust at the time of his death. Pierce stated that, if Vickie tried to get any of the assets, "it would be World War III." Indeed, the court finds that Pierce has adopted a scorched earth approach to the conduct of this litigation and has done his best to make it look like World War III.

III. Pierce's Discovery Abuses

The court previously found that Pierce engaged in massive discovery abuse in this adversary proceeding in connection with the production of documents properly requested under Rule 7034, which incorporates by reference Rule 34 of the Federal Rules of Civil Procedure.

Pierce's discovery infractions include four kinds of egregious discovery abuse. First, he failed to serve a written response within 30 days after the service of the request, as required by Rule 34(b) and

following respects: (1) this page alone lacks a watermark; (2) this page is missing a number of the staple holes that appear in the pages before and after, which result from a number of restaplings of the original document; and (3) this page was printed with a different printer from the rest of the document. This page, in its present form, was not part of the original document.

incorporated by reference in Fed.R.Bankr.P. 7034.[14] Second, more than a year after the document production request (and after monetary sanctions had been imposed more than once), Pierce provided a privilege log which listed thousands of documents that were not produced based on claims of attorney-client privilege or work product. This privilege log was grossly insufficient for supporting his claim that the documents were not subject to discovery. Third, Pierce disobeyed altogether the court's order to submit these documents for examination in chambers to determine whether the documents qualified for discovery exemption. Fourth, Pierce destroyed a substantial quantity of documents that were subject to a pending discovery request. These egregious discovery abuses require that the court impose appropriate sanctions.[15]

A. Sending Documents to Attorney

Pierce testified that, upon J. Howard's death, he boxed up all of J. Howard's papers and sent them to Edwin Hunter in Lake Charles, Louisiana. These papers fall into two categories: papers belonging to MPI and personal papers that belonged to J. Howard at the time of his death. For both categories, Pierce's

[14] Pierce also did not serve such a response at any reasonable time thereafter.

[15] These discovery abuses are not the only ones committed by Pierce, but only the most egregious.

obligation to produce the documents is the same as if they were still in his personal possession. As to the documents belonging to MPI, Pierce was the president and sole director of MPI at all material times during this litigation and had the power and responsibility to produce the documents.

As to the personal papers of J. Howard, Pierce was the administrator of J. Howard's probate estate in Louisiana when this adversary proceeding began,[16] when the document production requests were promulgated, when responses thereto came due, and when the documents should have been produced. The Louisiana probate case was ultimately dismissed for lack of jurisdiction and a new probate case was filed in Texas, where a different administrator was appointed. However, Pierce's default occurred during his watch, and his failure to produce the documents cannot be excused by his subsequent replacement by another administrator. Furthermore, the court is informed that Pierce's successor eventually waived any privilege that he had in the documents. Nonetheless, the documents were never produced in this adversary proceeding.

It is hornbook law that delivering pre-existing documents to a lawyer does not change a party's

[16] This adversary proceeding began as a claim that Pierce filed in this bankruptcy case for defamation, and Vickie's counterclaim that is the subject of this decision. Summary judgment was previously awarded to Vickie on the defamation claim, because Pierce offered no evidence to support the claim.

obligation to produce them in litigation. McCormick states:

> [T]his principle is controlling: If a document would be subject to an order for production if it were in the hands of the client it will be equally subject to such an order if it is in the hands of his attorney.

MCCORMICK ON EVIDENCE 330 (John William Strong, ed., 4th ed.1992); *accord, United States v. Robinson,* 121 F.3d 971, 975 (5th Cir.1997) ("it goes without saying that documents do not become cloaked with the lawyer-client privilege merely by the fact of their being passed from client to lawyer"); *Smith v. Texaco, Inc.,* 186 F.R.D. 354, 356-57 (E.D.Tex.1999). McCormick further states that any other rule "would be an intolerable obstruction to justice." MCCORMICK, *supra,* at 329.

Pierce had full responsibility for the production of all documents in either of these two categories that he sent to Hunter. When Vickie made demand for the production of the documents, Pierce's responsibility was to instruct Hunter to produce the documents for inspection or copying, or to raise any claimed defense to their discovery in a timely filed response. Hunter did neither.[17]

[17] If, after receiving such instructions, Hunter failed or refused to produce the documents, Pierce's remedy is against Hunter for violation of Hunter's duty as Pierce's agent to obey his lawful orders.

B. Claiming a Privilege

A party claiming a privilege has the burden of showing that the privilege applies. *United States v. Bauer,* 132 F.3d 504, 507 (9th Cir.1997). Federal common law governs the application of a privilege in an adjudication based on federal law. *See* Fed.R.Evid. 501. Where state law provides the applicable substantive law, privilege issues are governed by that state's law. *Id.* In this case, the causes of action at issue are governed by Texas law. Thus Texas law governs the issues of attorney-client privilege and work product.

The legal standard for the attorney-client privilege is as follows:

> (1) Where legal advice of any kind is sought (2) from a professional legal adviser in his capacity as such, (3) the communications relating to that purpose, (4) made in confidence (5) by the client, (6) are at his instance permanently protected (7) from disclosure by himself or by his legal advisor, (8) except the protection be waived.

See 8 J. WIGMORE, EVIDENCE § 2292 at 554 (J. McNaughton rev.1961); *see also United States v. El Paso Co.,* 682 F.2d 530, 538 (5th Cir.1982); *Smith v. Texaco, Inc.,* 186 F.R.D. 354, 356 (E.D.Tex.1999).

For each document transmitted to a non-attorney, Pierce must show, as to each such recipient, (a) the recipient's name, (b) the position that the recipient held at the time, (c) if the recipient received the document as a corporate official or employee, how the

corporation's privilege applied to the recipient. *See Upjohn Co. v. United States,* 449 U.S. 383, 391-96, 101 S.Ct. 677, 683-86, 66 L.Ed.2d 584 (1981).

Pierce has not made an adequate showing on any of these issues, as to any of the documents at issue. While the names of some of the authors and recipients are given, none is identified as an attorney. The positions of the non-attorneys at the relevant times are not given, nor is any explanation given of how they qualify under *Upjohn.*

The court has serious reservations about the legitimacy of the attorney-client privilege and work product claims. Pierce did deliver more than 100 documents for *in camera* inspection that were in the possession of Jeff Townsend. The court found that approximately 13 of the documents were subject to a legitimate claim of attorney-client privilege or work product. For most of the remaining documents, the court found no good faith contention that either exception applied. The non-qualifying documents included such items as transmittal letters, annual statements of KII, a videotape of J. Howard's arrival at Vickie's home to visit her after their marriage, and photographs of Vickie taken on vacation after J. Howard's death. The court infers from this evidence that most of the attorney-client privilege and work

product claims for the Hunter documents are equally meritless.[18]

Because Pierce failed to carry the burden of showing the applicability of either the attorney-client privilege or the attorney work product doctrine, all of the documents on the privilege log should have been produced to Vickie in this litigation. They were not. The court concludes and finds that all of the privilege and work product claims relating to the Hunter documents were also specious and made in bad faith.

C. Sanctions for Discovery Violations

The court issued its findings and sanctions order on the discovery violations on May 20,

[18] If Ninth Circuit law had governed the procedures relating to the testing of the assertion of attorney-client privilege and work product, that law would require the party opposing the privilege claim to show a factual basis sufficient to support a reasonable, good faith belief that *in camera* inspection may reveal evidence that information in the materials is not privileged. *See In re Grand Jury Investigation,* 974 F.2d 1068, 1074-75 (9th Cir.1992); *see also United States v. Zolin,* 491 U.S. 554, 572, 109 S.Ct. 2619, 2631, 105 L.Ed.2d 469 (1989) (for determination of crime-fraud exception to attorney-client privilege, once threshold showing is made, court has discretion to conduct *in camera* review based on all the facts and circumstances of the case, including the relative importance to the case of the alleged privileged information, the likelihood that the evidence produced through *in camera* review (together with the other evidence in the case) will establish that the exception applies). The experience with the Townsend documents fully satisfies these requirements.

1999.[19] The court subsequently vacated that order. Meanwhile, Pierce has done nothing to vitiate his refusal to produce the documents at issue for an *in camera* inspection.

The findings of fact and conclusions of law highlighted in bold in this opinion or otherwise specified are imposed as sanctions for Pierce's discovery abuse. The court finds that many documents listed in the privilege log directly relate to the transactions as to which the sanctions are imposed. Furthermore, there is no way to know what was in the documents that Pierce destroyed while they were subject to a discovery request.

In addition, Edwin Hunter testified at the trial over Vickie's objections based on Hunter's failure to produce the Hunter documents or to submit them to the court for *in camera* inspection. The court now sustains those objections, and strikes Hunter's testimony.

IV. Tortious Interference with Expectancy of Inheritance or Gift

Texas law clearly recognizes tortious interference with an inheritance or gift as a valid cause of action. The leading Texas case is *King v. Acker,* 725 S.W.2d 750, 754 (Tex.App.1987); *see also Brandes v. Rice*

[19] The court issued a prior set of findings and sanctions on January 21, 1999, which were vacated by the district court and remanded for more specific findings.

Trust, Inc., 966 S.W.2d 144, 146-47 (Tex.App.1998). In *King* the court sustained a claim for tortious interference with an expected inheritance in an action brought against the decedent's second wife by the decedent's two children from his first marriage. The court found that the second wife improperly attempted to assign 500 shares of stock to herself from the decedent while he was in a coma, pursuant to a power of attorney that the jury found the decedent had not signed.

King was the first published opinion declaring that Texas law recognizes a cause of action for tortious interference with inheritance rights. Following courts from other states, the court relied on the Restatement formulation of the rule, which states:

> One who by fraud, duress or other tortious means intentionally prevents another from receiving from a third person an inheritance or gift that he would otherwise have received is subject to liability to the other for loss of the inheritance or gift.

Restatement (Second) of Torts § 774B (1977). The court further supported its conclusion by stating:

> It is well understood that the law affords a remedy for every invasion of a legal right. Under the maxim "where there is a right, there is a remedy," equity will not suffer a right to be without a remedy.

King, 725 S.W.2d at 754. On these grounds the court upheld an award of both compensatory and punitive

damages against the decedent's second wife for using the forged power of attorney to transfer stock from the decedent to herself while he was unconscious.

In *Brandes* the decedent's sister and her children brought an action against Rice University for tortiously interfering with their expectancy to inherit some $4 million in municipal bonds that the decedent transferred to the university on his deathbed. The court ruled for the university because the decedent's will would not have left the bonds to the plaintiffs if the transfer to the university had not been made. *Brandes*, 966 S.W.2d at 149.

Texas case law does not specify the elements of a cause of action for tortious interference with an expectancy of inheritance or gift. Other jurisdictions, however, have generally held that a plaintiff must prove the following five elements: (1) the existence of an expectancy; (2) a reasonable certainty that the expectancy would have been realized, but for the interference; (3) intentional interference with that expectancy; (4) tortious conduct involved with the interference; and (5) damages. *See, e.g., Doughty v. Morris*, 117 N.M. 284, 871 P.2d 380, 384 (Ct.App.1994); *see also* James A. Fassold, *Tortious Interference with Expectancy of Inheritance: New Tort, New Traps*, ARIZ. ATT'Y, 26, 27 (Jan.2000); Dennis D. Reaves, *Tortious Interference with an Expected Gift or Inheritance*, J.MO.B. 563, 564 (1991).

A. Existence of an Expectancy

The court finds that Vickie had an expectancy to receive a substantial portion of J. Howard's wealth. J. Howard repeatedly told her that she would receive half of what he owned. While J. Howard never made a will with any provision for her, this was because his principal assets were already in the Living Trust. J. Howard's plan was to provide for Vickie from the Living Trust.

In December, 1992 J. Howard instructed both Sorensen and Hunter to arrange a gift to Vickie from the Trust. J. Howard instructed Hunter, a tax and estate planning expert, to prepare a "catch-all trust" for Vickie. A few days later J. Howard instructed Sorensen to prepare the documents for a gift to Vickie of one-half of the future appreciation in J. Howard's interest in the MPI stock. No evidence has been offered that these instructions were ever rescinded.

B. Reasonable Certainty of Expectancy But For Defendant's Conduct

Vickie must show with a reasonable degree of certainty that she would have received the expectancy but for Pierce's interference. Comment d to § 774B states in relevant part:

> [T]here must be proof amounting to a reasonable degree of certainty that the bequest or devise would have been in effect at the time of the death of the testator or that the gift would have been made inter vivos if there

> had been no such interference. . . . Complete certainty is [often] impossible. It is not required. . . . The fact that it was the defendant's tortious act that makes it not possible to prove with certainty may be taken into consideration by the court.

RESTATEMENT, *supra*, cmt. d.

No evidence has been presented on why J. Howard's instructions to Sorensen and Hunter were not followed. The court assumes that the answers to this question lie in the documents that Pierce has destroyed or refused to produce. **The court finds that the gift to provide for Vickie did not take place because Pierce fired Sorensen and conspired with Hunter to prevent the drafting and execution of the documents that would have accomplished the gift that J. Howard directed.**

Thus Vickie has adequately shown the reasonable certainty that she would have received a substantial gift from J. Howard, in the amount that the court hereafter awards as damages.

C. Intentional Conduct

Tortious interference with an expectancy is an intentional tort. A plaintiff must show an intentional invasion or destruction of plaintiff's prospective interest or expectancy of which the defendant had actual knowledge. Reaves, *supra,* at 564. The proof must show that the defendant was aware of his or her

interference and in fact intended to interfere with the expectancy. Marilyn Marmai, Note, *Tortious Interference With Inheritance: Primary Remedy or Last Recourse,* 5 Conn.Prob.L.J. 295, 301 (1991).

When Pierce learned of J. Howard's directions to arrange a trust for Vickie in December 1992, he took action with Hunter to prevent the formation of the trust and the transfer of assets from the Living Trust for Vickie's benefit. Furthermore, in July 1994, upon learning of his father's marriage to Vickie, Pierce acted to assure that the marriage did not interfere with his own expectation that he and his family would inherit all of his father's wealth. There is no doubt that this conduct was intentional and specifically intended to prevent Vickie from obtaining any of the Marshall interest in MPI and KII.

Hunter, acting on **Pierce's instructions**, failed to prepare the catch-all trust. In addition, in 1994, **again acting on Pierce's** instructions, Hunter devised a plan to make the Living Trust irrevocable and prepared the Fine Tuning Document to permit this to take place. After J. Howard apparently signed the Fine Tuning Document, Pierce caused the Document to be altered to substitute the page that made the Living Trust irrevocable. Whether in fact the Fine Tuning Document is genuine and effective to carry out this purpose will be decided by the Probate Court in Texas.

D. Independently Tortious Conduct

The most important element of tortious interference with the expectancy of an inheritance is that the defendant's conduct must be tortious. Typical examples of this tort occur where a testator has been induced to make or not to make a bequest by fraud, duress, defamation or tortious abuse of fiduciary duty, or the tortfeasor has forged, altered or suppressed a will (or a document making a gift). RESTATEMENT § 774B, *supra,* cmt. c; *see also* Fassold, *supra,* at 27. In contrast, persuading a testator to eliminate an expectancy through legitimate means is not enough to satisfy this element. *See* Reaves, *supra,* at 564.

Pierce's tortious conduct in this case came in two phases. **First, at the end of 1992 and in early 1993 he fired Sorensen for the purpose of preventing him from arranging the gift to Vickie of the increase in value of the MPI stock, and he conspired with Hunter to prevent the preparation of the catch-all trust.** Second, he caused the altering of the Fine Tuning Document, by substituting a new second page of the document after its apparent execution to insert a provision that purported to make the Living Trust irrevocable. This independently tortious conduct supports Vickie's claim for tortious interference with her expectancy of an inheritance from her deceased husband J. Howard.

E. Damages

Vickie offers three different measures of damages for Pierce's wrongful conduct. First, she contends that the court should award damages that equal half of everything in which J. Howard had an interest. According to Vickie's expert Wayne Elggren,[20] half of J. Howard's interest in MPI, as of August 31, 1999 (immediately before the trial in this adversary proceeding), was worth $820,489,480. This amount would give effect to J. Howard's repeated promise that she would get half of what he had.

As a second possible measure of damages, Elggren testified that J. Howard's share of the appreciation in the KII stock from December 23, 1992 to August 31, 1999 was $556,874,869. This sum would give effect to J. Howard's instructions to Sorensen on or about that date to arrange a structure to give Vickie the appreciation in value of J. Howard's interest in the KII stock.

Elggren presented a third possible measure of damages, the increase in value of the MPI stock from June 27, 1994, the date of Vickie and J. Howard's marriage, to August 31, 1999. Elggren testified that the J. Howard's interest in the MPI stock increased during this period from $741,470,693 to $1,640,978,961, an increase of $899,508,268. Vickie's half share of this sum would be $449,754,134.

[20] The court finds all of Elggren's testimony on this subject to be credible.

Pierce's expert Mike Hill opined that the community property value of the KII stock was $170 million. **The court denied the admission of Hill's testimony as sanctions for Pierce's discovery violations, as discussed *supra* and as provided in the court's order of May 21, 1999.**

The court finds the most appropriate measure of Vickie's damages from Pierce's tortious interference with her expectancy of a gift from J. Howard to be the lowest of these figures, $449,754,134. While J. Howard gave the instructions to make the gift in 1992, the court finds that J. Howard gave this direction in contemplation that Vickie would marry him. In fact she did, but not until 1994. The court finds it equitable to measure her damages from the date of their marriage.

Vickie has actually been damaged only to the extent that she does not receive a share of the probate estate in Texas. The probate action is in trial now, and the amount that Vickie receives in that proceeding must be deducted to determine the damages that Pierce has caused.

F. Punitive Damages

Under Texas law, damages available for the tortious interference with an expectancy of an inheritance or gift may include consequential damages, emotional distress or actual harm to reputation, and punitive damages. *See King,* 725 S.W.2d at 754; *see also* Fassold, *supra,* at 29; Reaves, *supra,* at 565.

Vickie has not shown any consequential damages, emotional distress or harm to reputation. However, she does claim punitive damages against Pierce.

It appears to the court that, under Texas law, this is an appropriate case for the assessment of punitive damages. However, the determination of the amount of punitive damages must await the calculation of the compensatory damages. This calculation, in turn, must await the determination of the amount, if any, that Vickie receives from J. Howard's estate.

V. Conclusion

The court concludes that Vickie has shown, by a preponderance of the evidence admitted at trial and the findings imposed as sanctions against Pierce for discovery abuses, that Pierce has tortiously deprived her of her expectancy of a substantial *inter vivos* gift from her deceased husband J. Howard.

The court awards damages in the amount of $449,754,134, less any amount that Vickie actually recovers in the pending Probate Court action in Texas. In addition, Vickie is entitled to punitive damages in an amount that remains to be determined after her actual damages are calculated.

NOT FOR PUBLICATION

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

In the Matter of: VICKIE LYNN MARSHALL, Debtor, ELAINE MARSHALL, as Independent Executor of the Estate of E. Pierce Marshall, Plaintiff Counter-Defendant/ Appellant-Cross-Appellee, v. HOWARD K. STERN, as Executor under the Will of Vickie Lynn Marshall, Defendant-Counter-Claimant/ Appellee Cross-Appellant.	No. 02-56002, 02-56067 D.C. No. CV-01-00097-DOC Central District of California, Santa Ana ORDER (Filed May 5, 2010)

Before: BEEZER, KLEINFELD and PAEZ, Circuit Judges.

The panel has voted to deny the petition for panel rehearing. Judges Kleinfeld and Paez vote to deny the petition for rehearing en banc and Judge Beezer so recommends.

The full court has been advised of the petition for rehearing en banc and no judge has requested a vote to rehear the matter en banc. Fed. R. App. P. 35.

The petition for panel rehearing and the petition for rehearing en banc are DENIED.

U.S. Const. art. I § 8

Article I

Section 8.

The Congress shall have Power . . .

To establish an uniform Rule of Naturalization, and uniform Laws on the subject of Bankruptcies throughout the United States;

. . .

To make all Laws which shall be necessary and proper for carrying into Execution the foregoing Powers, and all other Powers vested by this Constitution in the Government of the United States, or in any Department or Officer thereof.

U.S. Const. art. III

Article III

Section 1.

The judicial Power of the United States, shall be vested in one supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish. The Judges, both of the supreme and inferior Courts, shall hold their Offices during good Behaviour, and shall, at stated Times, receive for their Services, a Compensation, which shall not be diminished during their Continuance in Office.

Section 2.

The judicial Power shall extend to all Cases, in Law and Equity, arising under this Constitution, the Laws of the United States, and Treaties made, or which shall be made, under their Authority; – to all Cases affecting Ambassadors, other public ministers and Consuls; – to all Cases of admiralty and maritime Jurisdiction; – to Controversies to which the United States shall be a Party; – to Controversies between two or more States; – between a State and Citizens of another State; – between Citizens of different States, – between Citizens of the same State claiming Lands under Grants of different States, and between a State, or the Citizens thereof, and foreign States, Citizens or Subjects.

In all Cases affecting Ambassadors, other public Ministers and Consuls, and those in which a State shall be Party, the supreme Court shall have original Jurisdiction. In all the other Cases before mentioned, the supreme Court shall have appellate Jurisdiction, both as to Law and Fact, with such Exceptions, and under such Regulations as the Congress shall make.

The Trial of all Crimes, except in Cases of Impeachment, shall be by Jury; and such Trial shall be held in the State where the said Crimes shall have been committed; but when not committed within any State, the Trial shall be at such Place or Places as the Congress may by Law have directed.

Section 3.

Treason against the United States, shall consist only in levying War against them, or in adhering to their Enemies, giving them Aid and Comfort. No Person shall be convicted of Treason unless on the Testimony of two Witnesses to the same overt Act, or on Confession in open Court.

The Congress shall have Power to declare the Punishment of Treason, but no Attainder of Treason shall work Corruption of Blood, or Forfeiture except during the Life of the Person attainted.

STATUTES INVOLVED

The statutes relevant to the present petition are set forth in full as follows.

A. 28 U.S.C. § 157 (2006)

(a) Each district court may provide that any or all cases under title 11 and any or all proceedings arising under title 11 or arising in or related to a case under title 11 shall be referred to the bankruptcy judges for the district.

(b)(1) Bankruptcy judges may hear and determine all cases under title 11 and all core proceedings arising under title 11, or arising in a case under title 11, referred under subsection (a) of this section, and may enter appropriate orders and judgments, subject to review under section 158 of this title.

(2) Core proceedings include, but are not limited to –

> **(A)** matters concerning the administration of the estate;
>
> **(B)** allowance or disallowance of claims against the estate or exemptions from property of the estate, and estimation of claims or interests for the purposes of confirming a plan under chapter 11, 12, or 13 of title 11 but not the liquidation or estimation of contingent or unliquidated personal injury tort or wrongful death claims against the estate for purposes of distribution in a case under title 11;

(C) counterclaims by the estate against persons filing claims against the estate;

(D) orders in respect to obtaining credit;

(E) orders to turn over property of the estate;

(F) proceedings to determine, avoid, or recover preferences;

(G) motions to terminate, annul, or modify the automatic stay;

(H) proceedings to determine, avoid, or recover fraudulent conveyances;

(I) determinations as to the dischargeability of particular debts;

(J) objections to discharges;

(K) determinations of the validity, extent, or priority of liens;

(L) confirmations of plans;

(M) orders approving the use or lease of property, including the use of cash collateral;

(N) orders approving the sale of property other than property resulting from claims brought by the estate against persons who have not filed claims against the estate;

(O) other proceedings affecting the liquidation of the assets of the estate or the adjustment of the debtor-creditor or the equity security holder relationship, except personal injury tort or wrongful death claims; and

(P) recognition of foreign proceedings and other matters under chapter 15 of title 11.

(3) The bankruptcy judge shall determine, on the judge's own motion or on timely motion of a party, whether a proceeding is a core proceeding under this subsection or is a proceeding that is otherwise related to a case under title 11, A determination that a proceeding is not a core proceeding shall not be made solely on the basis that its resolution may be affected by State law.

(4) Non-core proceedings under section 157(b)(2)(B) of title 28, United States Code, shall not be subject to the mandatory abstention provisions of section 1334(c)(2).

(5) The district court shall order that personal injury tort and wrongful death claims shall be tried in the district court in which the bankruptcy case is pending, or in the district court in the district in which the claim arose, as determined by the district court in which the bankruptcy case is pending.

(c)(1) A bankruptcy judge may hear a proceeding that is not a core proceeding but that is otherwise related to a case under title 11. In such proceeding, the bankruptcy judge shall submit proposed findings of fact and conclusions of law to the district court, and any final order or judgment shall be entered by the district judge after considering the bankruptcy judge's proposed findings and conclusions and after reviewing de novo those matters to which any party has timely and specifically objected.

(2) Notwithstanding the provisions of paragraph (1) of this subsection, the district court, with the consent of all the parties to the proceeding, may refer a proceeding related to a case under title 11 to a bankruptcy judge to hear and determine and to enter appropriate orders and judgments, subject to review under section 158 of this title.

(d) The district court may withdraw, in whole or in part, any case or proceeding referred under this section, on its own motion or on timely motion of any party, for cause shown. The district court shall, on timely motion of a party, so withdraw a proceeding if the court determines that resolution of the proceeding requires consideration of both title 11 and other laws of the United States regulating organizations or activities affecting interstate commerce.

(e) If the right to a jury trial applies in a proceeding that may be heard under this section by a bankruptcy judge, the bankruptcy judge may conduct the jury trial if specially designated to exercise such jurisdiction by the district court and with the express consent of all the parties.

B. 28 U.S.C. § 1331 (2006)

The district courts shall have original jurisdiction of all civil actions arising under the Constitution, laws, or treaties of the United States.

C. 28 U.S.C. § 1334 (2006)

(a) Except as provided in subsection (b) of this section, the district courts shall have original and exclusive jurisdiction of all cases under title 11.

(b) Except as provided in subsection (e)(2), and notwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the district courts, the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11.

(c)(1) Except with respect to a case under chapter 15 of title 11 [11 USCS §§ 1501 et seq.], nothing in this section prevents a district court in the interest of justice, or in the interest of comity with State courts or respect for State law, from abstaining from hearing a particular proceeding arising under title 11 or arising in or related to a case under title 11.

(2) Upon timely motion of a party in a proceeding based upon a State law claim or State law cause of action, related to a case under title 11 but not arising under title 11 or arising in a case under title 11, with respect to which an action could not have been commenced in a court of the United States absent jurisdiction under this section, the district court shall abstain from hearing such proceeding if an action is commenced, and can be timely adjudicated, in a State forum of appropriate jurisdiction.

(d) Any decision to abstain or not to abstain made under subsection (c) (other than a decision not to abstain in a proceeding described in subsection (c)(2)) is not reviewable by appeal or otherwise by the court of appeals under section 158(d), 1291, or 1292 of this title [28 USCS § 158(d), 1291, or 1292] or by the Supreme Court of the United States under section 1254 of this title [28 USCS § 1254]. Subsection (c) and this subsection shall not be construed to limit the applicability of the stay provided for by section 362 of title 11, United States Code, as such section applies to an action affecting the property of the estate in bankruptcy.

(e) The district court in which a case under title 11 is commenced or is pending shall have exclusive jurisdiction –

(1) of all the property, wherever located, of the debtor as of the commencement of such case, and of property of the estate; and

(2) over all claims or causes of action that involve construction of section 327 of title 11, United States Code [11 USCS § 327], or rules relating to disclosure requirements under section 327 [11 USCS § 327].

Case Nos. 02-56002, 02-56067

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

In re: VICKIE LYNN MARSHALL,
Debtor.

ELAINE T. MARSHALL, EXECUTRIX OF THE ESTATE OF E. PIERCE MARSHALL,
Appellant and Cross-Appellee,

v.

HOWARD K. STERN, EXECUTOR OF THE ESTATE OF VICKIE LYNN MARSHALL,
Appellee and Cross-Appellant.

Appeal from Decision of the
United States, District Court
Central District of California
Case No. Case No. SA CV-01-00097
(Honorable David O. Carter, Judge)

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PETITION FOR REHEARING
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INTRODUCTION

In 2006, the Supreme Court reversed this Circuit's holding in this case that the probate exception barred the federal courts from hearing Vickie Lynn Marshall's counterclaim for tortious interference with gift filed against Pierce Marshall's

proof of claim for defamation. *Marshall v. Marshall*, 547 U.S. 293, 314-15 (2006).[1]

On remand, the motions panel that previously reversed the district court's decision in Vickie's favor has done so again. Opn:4534-35.[2] This time it has held that Vickie's compulsory counterclaim was not a core proceeding under 28 U.S.C. §157(b)(2)(C) and therefore the bankruptcy court's judgment was not "final," and a later judgment in a Texas probate court entered while the district court was reviewing the bankruptcy court ruling should be given issue-preclusive effect. Opn:4527-28, 4534-35.

En banc review is necessary because the Opinion creates a circuit split on exceptionally important constitutional and statutory questions in which there

[1] Both original parties are now deceased. Following the Opinion, we refer to Vickie and Pierce as though still the current parties.

[2] After a briefing schedule was ordered in this appeal, Pierce filed a motion for summary reversal with the then-current motions panel, which *sua sponte* ordered expedited briefing on the merits. 9thCir.Doct.Nos. 22, 51. Over two years later, the motions panel denied Pierce's motion and issued its probate-exception opinion. *In re Marshall*, 392 F.3d 1118, 1137 n.16 (9th Cir. 2004). After the Supreme Court reversed, Vickie moved to regularize the appeal, including assignment to a randomly-assigned merits panel to hear the remaining issues. 9thCir.Doct.No. 143; cf. former 9th Cir. R. 3-3(d); *Monterey Mech. Co. v. Wilson*, 138 F.3d 1270, 1271 (plurality), 1274 n.3 (Reinhardt, J., dissenting) (9th Cir. 1998); *Int'l Soc'y for Krishna Consciousness of Cal. Inc. v. City of L.A.*, 530 F.3d 768, 773 (9th Cir. 2008). Vickie's motion was never ruled on.

is an overriding need for national uniformity, and its breadth will fundamentally change indeed, confound everyday bankruptcy practice within this Circuit. The Opinion holds that even though Vickie's tortious interference counterclaim was a compulsory counterclaim to Pierce's creditor's claim for defamation, and that success on her counterclaim would defeat Pierce's claim, her counterclaim was non-core based on the constitutional limitations set forth in *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982) (plurality opinion) *(Marathon)*.

Although *Marathon* did not involve a counterclaim to a proof of claim or the revamped *post-Marathon* bankruptcy scheme, the Opinion relies on *Marathon* to announce a new rule that bankruptcy courts have no core jurisdiction over *any* compulsory counterclaim even one that could defeat the creditor's claim unless resolving the counterclaim is a necessary predicate to the allowance/disallowance of the creditor's claim and it raises no issue outside the creditor's claim. En banc review should be granted because the Opinion:

- Conflicts with the uniform rule of every Circuit that has considered the issue that core jurisdiction exists over any compulsory counterclaim to a creditor's claim.

- Ignores that Congress rectified *Marathon's* separation of powers concerns, including making

bankruptcy courts units of the district courts with their judges appointed by Article III judges.

- Ignores and contravenes a key post-Marathon Supreme Court decision upholding the constitutionality of a statutory scheme allowing non-Article III judges to decide compulsory counterclaims.

- Contravenes Congress' intent in enacting 28 U.S.C. §157(b); indeed, renders the statute's counterclaim provision superfluous.

- Creates the absurd result that debtors *must* file compulsory counterclaims in bankruptcy courts that then cannot finally decide them.

- Effects a sea change in Ninth Circuit bankruptcy practice that will undermine efficient bankruptcy administration by saddling courts with jurisdictional battles and splintering inextricably-linked claims between bankruptcy and district courts.

Panel review is also necessary because the Opinion overlooks Vickie's argument that the district court properly exercised its discretion to deny issue preclusion on fundamental fairness grounds. The Opinion holds that Pierce established all elements of preclusion, but the fairness inquiry is independent of whether the issue-preclusion elements are present.

THE OPINION

Core/Non-Core: The Opinion holds that determination of whether a counterclaim to a creditor's

claim is core under 28 U.S.C. §157(b)(2)(C) "must focus largely on what is available to the court at the time of filing, that is, the parties' pleadings." Opn:4525. Those pleadings generally alleged:

Pierce's creditor's claim: Vickie, through attorneys, defamed him to extort a settlement by making false media statements that he had used "forgery, fraud or over-reaching" to "wrongfully . . . steal control" of her husband Howard's assets, and that she was entitled to half of Howard's earnings during marriage. Opn:4496-98 & n.11; OpnAppx:4551-52.

Vickie's counterclaim: Pierce, in fact, "engag[ed] in a concerted campaign" through "fraud, duress and undue influence" to wrongly transfer Howard's property "inconsistent with his expressed wishes" and interfered with her expectancy. Opn:4521-22, 4526-27 & n.31; SER 6739-40.

The Opinion holds that Vickie's counterclaim was a compulsory counterclaim to Pierce's defamation claim "because the 'operative facts underlying [her] action' are the same as those underlying [Pierce's] defamation claim" and that "[t]he defamation claim, [Vickie's] affirmative defense of truth, and her counterclaim for tortious interference all concern the alleged efforts by [Pierce] to obtain control of his father's estate" through improper means. Opn:4521-22 & n.29. It also holds that core jurisdiction can exist over state law counterclaims such as Vickie's. Opn:4518-19 & n.27.

Nonetheless, the Opinion holds that Vickie's compulsory counterclaim is non-core because *Marathon* compels the following test: A compulsory counterclaim is a core proceeding under §157(b)(2)(C) only if "'the resolution of the counterclaim is necessary to resolve the allowance or disallowance of the claim itself.'" Opn:4524.

Applying this new test, the Opinion holds Vickie's compulsory counterclaim was non-core because it "was not a necessary predicate to the bankruptcy court's decision to allow or disallow [Pierce's] defamation claim" because the "defamation claim could be fully adjudicated without fully adjudicating [her] tortious interference claim." Opn:4524-27. It emphasizes that even if Vickie showed the statements underlying the defamation claim were true (which would defeat Pierce's creditor claim), she would have to prove additional factual elements to establish her counterclaim, such as the amount of damages from Pierce's tortious conduct. Opn:4527. Thus, while the Opinion recognizes that Vickie's success on her counterclaim would necessarily defeat Pierce's creditor's claim by establishing the affirmative defense of truth, it concludes that is not enough to confer core jurisdiction. *Id.*[3]

[3] The concurrence identifies "alternative" grounds for reversal, but each rests on assertions the majority *rejected* and the record refutes. Opn:4538. (Kleinfeld, J., concurring.)

• The concurrence states Pierce only sought a non-dischargeability determination, not damages from the bankruptcy estate. *Id.* The majority rejected that contention. Opn:4498 n.11.

(Continued on following page)

Preclusion: After concluding Vickie's counterclaim was non-core and her bankruptcy judgment thus not final, the Opinion reverses the district court judgment on the ground that "[a]ll of the elements of issue preclusion have been met in this case" and the Texas probate court findings prevent Vickie from establishing her tortious interference counterclaim. Opn:4490, 4528, 4534. But the Opinion overlooks Vickie's argument that the district court properly exercised its discretion to deny issue preclusion for fundamental fairness reasons, a ground that applies even when all issue-preclusion elements are met.

The record disproves it. SER:6801, 6101-02 (Pierce telling bankruptcy court that amount of his creditor's claim "shall be determined by the adversary proceedings filed herein" and he's "happy" to litigate "[his] claim here" because "we did choose this forum"), SER:8409-16 (Pierce estimating his claim at $8.5 million).

- The concurrence couches Vickie's counterclaim as an "evasion of Pierce's constitutional right to jury trial in Texas." Opn:4538. The majority held that Pierce *dismissed* his Texas defamation claim against Vickie after the bankruptcy filing. Opn:4496 n.10.

- The concurrence asserts there wasn't even "related to" jurisdiction because Vickie "had already been discharged and her creditors would get none of the money she sought from Pierce in her counterclaim." Opn:4538. The majority held that the bankruptcy plan specified that the counterclaim proceeds be applied first to creditor claims. Opn:4499.

I. EN BANC REVIEW IS NECESSARY BECAUSE THE OPINION'S RESTRICTIVE CONSTRUCTION OF BANKRUPTCY COURT CORE JURISDICTION OVER COMPULSORY COUNTERCLAIMS CREATES A CONFLICT WITH OTHER CIRCUITS, SUBVERTS CONGRESSIONAL INTENT AND FUNDAMENTALLY CHANGES AND CONFOUNDS BANKRUPTCY PRACTICE IN THIS CIRCUIT.

A. The Opinion's Restrictive Core Jurisdiction Analysis Contravenes Congress' Intent And Makes §157(b)(2)(C) Superfluous.

Marathon did *not* involve a *counterclaim* to a *proof of claim.* It held merely that "a non-Article III bankruptcy judge could not adjudicate a pre-petition contract dispute arising under state law *against a party that had not filed a proof of claim and was not otherwise related to the bankruptcy proceedings.*" *In re CBI Holding Co.,* 529 F.3d 432, 459 (2d Cir. 2008) (emphasis added).

Consistent with *Marathon's* narrow scope, Congress broadly defined core proceedings as those "arising under" the bankruptcy code and "arising in" bankruptcy cases and additionally specified in subsection (b)(2) of section 157, the "various types of proceeding *deemed by Congress* to be core proceedings." *In re Mankin,* 823 F.2d 1296, 1299 (9th Cir. 1987) (emphasis added); *accord In re Eastport Assocs.,* 935 F.2d 1071, 1076 (9th Cir. 1991) ("§157(b)

defines core proceedings as ones 'arising under title 11, or arising in a case under title 11,' and gives a nonexhaustive list of types of core proceedings"). Congress believed that *almost all proceedings* before bankruptcy judges the sponsors said 95% would be core. *In re Arnold Print Works, Inc.*, 815 F.2d 165, 168-69 (1st Cir. 1987); *Mankin*, 823 F.2d at 1301.

Congress specified in §157(b)(2)(C) that "counterclaims by the [bankruptcy] estate against persons filing claims against the estate" are core proceedings, thus demonstrating its intent that bankruptcy courts could enter judgment on those counterclaims. *See* §157(c)(1) (in non-core proceeding "otherwise related to" the bankruptcy case, bankruptcy judges can only make proposed findings).[4]

Congress thus understood and intended that while bankruptcy courts would have "related to" jurisdiction over state law claims against persons who had not filed proofs of claim (the *Marathon*

[4] The emergency bankruptcy rules enacted in *Marathon's* wake similarly specified that bankruptcy courts could not enter final judgments in "related proceedings" and that such proceedings included "claims brought by the estate against parties *who have not filed claims against the estate*" and "do *not* include . . . counterclaims by the estate in whatever amount against persons filing claims against the estate." *See In re Comm. of Unsecured Creditors of FS Commc'ns Corp.*, 760 F.2d 1194, 1200 (11th Cir. 1985) (emphasis added). §157's sponsors intended to codify those emergency rules. A&P 130 Cong. Rec. D338, at 1610, 1620, 1630; 130 Cong. Rec. 6045 (daily ed. March 20, 1984).

situation), core jurisdiction would exist over counterclaims to creditor claims because they arise in bankruptcy cases in connection with adjusting debtor-creditor relations. *See Marathon,* 458 U.S. at 71 (distinguishing "the restructuring of debtor-creditor relations, which is at the core of the federal bankruptcy power" from the contract claim at issue).

Since permissive counterclaims are not required to be asserted in bankruptcy cases, many courts have implied a permissive counterclaim exclusion to §157(b)(2)(C)'s unqualified language. But *compulsory* counterclaims to creditor claims *must* be filed in bankruptcy cases; otherwise, res judicata precludes their subsequent assertion. *In re Baudoin,* 981 F.2d 736, 741-44 (5th Cir. 1993).

The Opinion, by prohibiting core jurisdiction over a compulsory counterclaim unless it is necessary to determining allowance/disallowance of the creditor claim and raises no issues outside the claim, goes far beyond a mere implied limitation *it renders §157(b)(2)(C) entirely superfluous.* Congress already specified in §157(b)(2)(B) that core proceedings include the "allowance or disallowance of claims against the estate." If Congress had intended to limit core counterclaim jurisdiction to the allowance/disallowance of creditor claims, as the Opinion holds, the counterclaim provision would have been unnecessary.

But even the Opinion holds that "[w]e do not believe Congress intended §157(b)(2)(C) to be a

meaningless (or near meaningless) provision," warning "against construing a 'statute in a manner that is strained and, at the same time, would render a statutory term superfluous.'" Opn:4519. Yet, the Opinion's own restrictive construction of core compulsory counterclaim jurisdiction does exactly that.

This restrictive construction contravenes Congress' intent. As this Circuit has recognized, although the principle that courts should avoid constitutional problems may be apt in applying §157(b)(2)'s catch-all provisions (§157, subdivs. (b)(2)(A) and (b)(2)(0)), the more apt principle in applying its other provisions is that "the will of the legislature underlying the provision is not to be ignored." *Mankin,* 823 F.2d at 1301 n.3.

B. The Opinion Ignores That Congress Rectified *Marathon's* Separation Of Powers Concerns In The Present Bankruptcy Law.

The *Marathon* plurality partly based its decision on the threat of encroachment by the political branches on the judiciary's powers under the then-existing bankruptcy scheme. *See, e.g.,* 458 U.S. at 57-60, 64 n.15, 74, 83-84. Under that scheme, bankruptcy courts were independent of and required to exercise all of the jurisdiction conferred on the district courts, and bankruptcy judges were appointed by the political branches. *Id.* at 79 n.31, 84-87.

Congress then enacted the present statutory scheme, which as this Circuit recognized, was "for the specific purpose of curing the constitutional problems of the scheme under which *[Marathon]* arose." *Mankin,* 823 F.2d at 1306. Among the changes: district courts have *discretion* to delegate matters to bankruptcy courts and the power to withdraw previously referred matters, 28 U.S.C. §§1334(a), (b), 157(a), (d); bankruptcy courts are now units of the district courts, §151; and bankruptcy judges are appointed by Article III judges, §152. Under the new scheme, "there is less threat that exercise of 'judicial power' will be unduly influenced by the executive or legislative branches." *Mankin,* 823 F.2d at 1309.

C. The Opinion Conflicts With How Courts Nationwide Interpret §157(b)(2)(C), Including The Decades-Long Practice Of This Circuit's Courts.

The Opinion also conflicts with the overwhelming view essentially settled until this case that bankruptcy courts have core jurisdiction over compulsory counterclaims to creditor claims. That is the view of every Circuit that has addressed the issue and legions of lower courts within the other Circuits.[5]

[5] *See, e.g., In re C.W. Mining Co.,* No. 2:09 CV417DAK, slip op., 2009 WL 4906702 at *3 (D.Utah Dec. 11, 2009); *In re Mercer's Enters. Inc.,* 387 B.R. 681, 686 (Bankr.E.D.N.C. 2008); *In re Geneva Steel, LLC,* 343 B.R. 273, 277-78 (Bankr.D.Utah 2006); *In re Applied Thermal Sys., Inc.,* 294 B.R. 784, 787-89

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Until the Opinion, it also was the view of this Circuit's courts, which have recognized *for decades* that "[r]eason and precedent" compel the rule that "a debtor's counterclaim arising from the same transaction as the creditor's claim against the estate may be decided in the same manner as the claim." *In re Lion Country Safari, Inc. Cal.*, 124 B.R. 566, 569 (Bankr.C.D.Cal. 1991); *accord In re PNP Holdings Corp.*, 184 B.R. 805, 806 (B.A.P.9th Cir. 1995)), *aff'd*, 99 F.3d 910 (9th Cir. 1996) ("[i]t is well settled that a creditor consents to jurisdiction over related counterclaims by filing a proof of claim"); *In re Castlerock Props.*, 781 F.2d 159, 162 (9th Cir. 1986) (recognizing "well-settled law that a creditor consents to jurisdiction over related counterclaims by filing a proof of claim"); *In re County of Orange*, 203 B.R. 977, 980 (Bankr.C.D.Cal. 1996); *In re Marshland Dev., Inc.*, 129 B.R. 626, 631 n.10 (Bankr.N.D.Cal.1991); *In re Beugen*, 81 B.R. 994, 998-1000 (Bankr.N.D.Cal. 1988); *In re Sun W. Distribs.*, 69 B.R. 861, 863-65 (Bankr.S.D.Cal. 1987).

D. The Opinion Creates A Circuit Split.

The Opinion's compulsory counterclaim holding is contrary to every Circuit that has addressed the

(Bankr.N.D.Okla. 2003); *In re ABC-NACO, Inc.*, 294 B.R. 832, 837 (Bankr.N.D.Ill. 2003); *In re Asousa P'ship*, 276 B.R. 55, 66-72 (Bankr.E.D.Pa. 2002); *In re Norrell*, 198 B.R. 987, 994 n.4 (Bankr.N.D.Ala. 1996); *In re Nationwide Roofing & Sheet Metal*, 130 B.R. 768, 776 (Bankr.S.D.Ohio 1991).

issuc the First, Second and Fifth all of which have expressly upheld core jurisdiction over compulsory counterclaims to creditors' claims under §157(b)(2)(C) without qualification.

First Circuit: One week before the Opinion here, the First Circuit held in *In re American Bridge Products, Inc.,* F.3d , 2010 WL 797014 at *3 (1st Cir. 2010) that the bankruptcy court could adjudicate a trustee's counterclaims for negligence and breach of fiduciary duty against a receiver who filed a compensation claim because compulsory counterclaims to creditors' claims meet the statutory definition of core proceedings under §157(b)(2)(C). It did so even though the trustee sought damages for misfeasance, an issue beyond the mere allowance/ disallowance of the creditor's claim.

Second Circuit: In 2008, the Second Circuit upheld compulsory counterclaim jurisdiction under §157(b)(2)(C) where the debtor's auditor filed a proof of claim for $210,000 in unpaid pre-petition services for a 1994 audit, and the debtor's successor responded with compulsory contract and tort counterclaims, claiming the creditor committed malpractice from 1992 through 1994. *CBI,* 529 F.3d at 438, 441-42. The alleged malpractice was a defense to the creditor's claim, but the counterclaims also sought millions of dollars in malpractice damages relating to different years than those at issue in the creditor's claim. *Id.* at 461-62.

Holding the counterclaims core, the Second Circuit recognized that nothing in *Marathon* "'alters the basic principle that the filing of a proof of claim invokes the special rules of bankruptcy'" and thus counterclaims that are factually and legally connected to a proof of claim are core proceedings regardless whether they are based on state law, could have existed independently of the bankruptcy, are disproportionate to the creditor's claim or involve issues that are not a defense to the creditor's claim. *Id.* at 461-63 & n.12.

Fifth Circuit: In 1993, the Fifth Circuit held that a former debtor was required to have brought his lender liability claims as a counterclaim in bankruptcy against a former creditor who filed a claim based on the loans, because the former-debtor's claim would have been a core proceeding under §157(b)(2)(C). *Baudoin,* 981 F.2d at 741-42. It held the issue was whether a common nucleus of operative facts existed allowing the claims to be litigated together effectively, not whether the counterclaim, had it been brought, would have extinguished the creditor's claim. *Id.* at 743.

The facts of these cases show that none of the counterclaims was a necessary predicate to the decision to allow or disallow the creditor's claim and each involved issues beyond the allowance/disallowance decision. If the Opinion's new restrictive test for whether a counterclaim to a proof of claim is core under §157(b)(2)(C) is right, each of these Circuit cases would be wrong.

E. The Decision Ignores And Contravenes Supreme Court Authority Upholding Non-Article III Adjudication Of Counterclaims Arising Out Of The Same Transaction As The Claim.

In *Commodity Futures Trading Comm'n v. Schor*, 478 U.S. 833, 837, 850 (1986) *(Schor)*, the Supreme Court upheld the constitutionality of a statutory scheme that allowed customers to sue their commodity brokers before the Commodity Futures Trading Commission (CFTC), an Article I agency, and allowed the CFTC, in conformance with Congress's goal of efficient dispute resolution, to adjudicate counterclaims "'aris[ing] out of the transaction or occurrence or series of transactions or occurrences set forth in the complaint.'" *Id.*

The Supreme Court rejected the Court of Appeals' conclusion that *Marathon* prohibited the agency from adjudicating counterclaims based on state common law. *Id.* at 839-40. First, it recognized that the right to adjudication by an Article III judge is a personal right that can be waived by filing a claim in an Article I forum. *Id.* at 848-49. Second, it described *Katchen v. Landy*, 382 U.S. 323 (1966) as upholding "a bankruptcy referee's power to hear and decide state law counterclaims against a creditor who filed a claim in bankruptcy when those counterclaims *arose out of the same transaction*." *Schor*, 478 U.S. at 852 (emphasis added).

Given *Schor's* holding and its description of *Katchen,* the Opinion is wrong. Since the Opinion never mentioned *Schor,* it made no attempt to reconcile its restrictive interpretation of core jurisdiction with that case.

F. The Opinion's New Core Jurisdiction Test Flouts The Goal Of Efficient And Expeditious Bankruptcy Administration.

This Circuit has recognized "Congress's intent to reduce substantially the time-consuming and expensive litigation regarding a bankruptcy court's jurisdiction over a particular proceeding" and to ensure "the efficient and expeditious resolution of all matters connected to the bankruptcy estate." *In re Fietz,* 852 F.2d 455, 457 (9th Cir. 1988).

The Opinion flouts those objectives. It produces the absurd result that debtors must file compulsory counterclaims in bankruptcy courts that cannot finally adjudicate them. It will swamp bankruptcy and district courts with abstention and withdrawal motions, and spawn endless litigation and confusion over jurisdictional limits and claim and issue preclusion, since bankruptcy courts will have core jurisdiction over creditor claims, but legally and factually interconnected compulsory counterclaims may have to be decided in district court.

In short, the Opinion ensures that the confusion and complexity of this case will become the norm.

II. PANEL REHEARING IS REQUIRED BECAUSE THE OPINION OVERLOOKS VICKIE'S FUNDAMENTAL FAIRNESS ARGUMENT.

A. The Unaddressed Ground Would, If Affirmed, Preclude Reversal Because A District Court Has Discretion To Deny Issue Preclusion On Fairness Grounds Even If All Elements Of Issue Preclusion Are Present.

The Opinion reverses the district court judgment on the ground that "[a]ll of the elements of issue preclusion have been met" and thus Vickie is bound by Texas probate court findings that prevent her from establishing her counterclaim. Opn:4490, 4528, 4534. However, the Opinion's reversal is premature, as it did not address the district court's *independent* ground that to bind Vickie to the Texas court's findings would be fundamentally unfair. *In re Marshall*, 271 B.R. 858, 866 (C.D.Cal. 2001).[6]

[6] Vickie argued this issue in her original and supplemental briefing, Comb.Br:104-05; Supp.Br:48-52, and the Opinion notes that the district court had declined to apply issue preclusion as "inconsistent with the notion of fundamental fairness," Opn:4528 n.32.

B. The District Court Properly Exercised Its Discretion To Deny Issue Preclusion Based On Fundamental Fairness.

Courts have discretion to refuse to apply issue preclusion in the interest of fairness. *See* citations, Supp.Br:48. The district court recognized the unfairness of barring Vickie "from making her arguments in this [federal] forum, which was originally chosen by Pierce" and "is the only one she actively sought relief in." *Marshall,* 271 B.R. at 866. It stressed that Vickie "voluntarily dismissed her claims in the Texas Probate proceedings" and she no longer had any "motivation to litigate" her issues there. *Id.*

When her bankruptcy judgment became final, Vickie promptly filed it in the probate proceedings and nonsuited her claims there without prejudice. Supp.Br:4-6, 49. That should have been the end of her role in the Texas proceedings.[7] However, Pierce

[7] The Opinion quotes what it calls a "warning" to Vickie from the Texas court that once it entered judgment as to "who is entitled to [Howard's] Estate," her statutory right to refile her claim for tortious interference with a gift would be moot, because the Estate would be gone. Opn:4501. But Vickie's claim here was for damages against Pierce personally, and not for estate assets. The Texas court itself expressly disclaimed that it tried any "issue of tortious interference with inter vivos gift in this case at all" or decided any "complaints that [Vickie] has against [Pierce]" or any issues "to do with what complaints that [Vickie] has against [Pierce]." Supp.Br:43. It confirmed that Vickie's tortious interference claim was "not affected by [the

(Continued on following page)

dragged her back there by bringing new claims against her that evidenced his intention to relitigate issues already decided by the bankruptcy court. Supp.Br:49.

Vickie tried to stop this effort, but the Texas court refused to give full faith and credit to the bankruptcy judgment. The bankruptcy court enjoined Pierce from proceeding against Vickie in Texas on his new claims but relented on one claim in reliance on Pierce's assurances that it did not require the Texas court to relitigate any issues the bankruptcy court had decided. Supp.Br:49-50.

Pierce told the bankruptcy court he was litigating in Texas only "to ensure that the Texas Probate Court can determine all claimants and efficiently administer that estate." Supp.Br:50. Since she was not a claimant of Howard's Estate or Living Trust, and her federal judgment awarded her only damages against Pierce personally, she had no reason to believe the Texas court was relitigating the claim she had already won in federal court.

Pierce reneged on his representations when he moved in the district court to preclude Vickie's tortious interference counterclaim based on the Texas judgment. *Marshall,* 271 B.R. at 862. If the bankruptcy court could enjoin Pierce from bringing new

probate court judgment] at all" and was "still in court out there" in California. Supp.Br:36.

claims in Texas to avoid an inconsistent judgment, and Vickie could reasonably rely on his no-relitigation promises, the district court could on fairness grounds prevent Pierce from asserting that judgment to preclude Vickie's counterclaim and thus profiting from his misrepresentations.

Dated: April 7, 2010

Respectfully submitted,

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CERTIFICATE OF SERVICE

I am employed in the County of Los Angeles, State of California, am over the age of 18, and am not a party to the within action.

I certify that on **April 8, 2010**, I electronically filed the foregoing **APPELLEE'S/CROSS-APPELLANT'S PETITION FOR REHEARING AND REHEARING EN BANC** with the Clerk of the Court for the United States Court of Appeals for the Ninth Circuit by using the appellate CM/ECF system.

Participants in the case who are registered CM/ECF users will be served by the appellate CM/ECF system.

I further certify that some of the participants in the case are not registered CM/ECF users. I have mailed the foregoing document by First-Class mail, postage prepaid, to the following non-CM/ECF participants:

N/A

I enclosed a copy of the document in a sealed, addressed envelope and placed the envelope for collection and mailing in the United States mail at Los Angeles, California, following our ordinary business practices on the aforesaid date.

/s/ Leanna Sun Borys

CERTIFICATE OF COMPLIANCE

Pursuant to Fed. R. App. P. 32(a)(7)(C) and Ninth Circuit Rule 32-1 for Case Nos.02-56002, 02-56067

I certify that pursuant to Fed. R. App. P. 32(a)(7)(C) and Ninth Circuit Rule 32-1, the attached **APPELLEE'S/CROSS-APPELLANT'S PETITION FOR REHEARING AND REHEARING EN BANC** is proportionately spaced, has a typeface of 14 points or more and contains **4,198** words.

Dated:April 8, 2010

/s/ Alan Diamond

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UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA
LOS ANGELES DIVISION

In re	) CASE NO. LA 96-12510-SB
VICKIE LYNN MARSHALL,	) Chapter 11
Debtor.	) Adversary No. 96-01838 SB
E. PIERCE MARSHALL,	) ANSWER AND COUNTERCLAIM BY VICKIE LYNN MARSHALL AGAINST E. PIERCE MARSHALL UNDER 11 U.S.C. §§544, 550, AND APPLICABLE LAW
Plaintiff,	)
v.	)
VICKIE LYNN MARSHALL,	)
Defendant.	) (Filed June 14, 1996)
VICKIE LYNN MARSHALL,	) STATUS CONFERENCE
Counterclaimant,	) DATE: July 10, 1996
v.	) TIME: 10:00 a.m.
E. PIERCE MARSHALL,	) CTRM: 1575 Roybal Federal Building 255 East Temple Street Los Angeles, CA 90012
Counterdefendant.	)

* * *

SECOND AFFIRMATIVE DEFENSE

16. Answering further, the statements complained of in this action are in fact substantially true, in whole and in part, and, therefore cannot form the basis of a claim for libel.

* * *

COUNTERCLAIMS

I.

JURISDICTION AND PARTIES

1. Jurisdiction of this Court is founded upon 28 U.S.C. §§157 and 1334 in that this Answer and Counterclaim is a civil proceeding an adversary proceeding and a core proceeding arising under title 11 of the United States Code and arising in the above-captioned case under chapter 11 of title 11 of the United States Code filed and pending in the United States Bankruptcy Court for the Central District of California. Further, this Counterclaim includes pleadings and allegations that constitute a counterclaim, an avoidance action, a turn-over proceeding, and a complaint to enjoin actions taken in other states to defraud creditors and therefore is a core proceeding under 28 U.S.C. §157(b)(2)(C), (E), (H) and (O). Under 28 U.S.C. §1409(a), venue is appropriate in this Court as this adversary proceeding arises in the above-captioned chapter 11 case.

* * *

FOURTH COUNTERCLAIM

(Tortious Interference With Inheritance)

35. Mrs. Marshall incorporates by reference paragraphs 1 through 25, as though fully set forth.

36. By the promises made to Mrs. Marshall, by the intentions expressed by Mr. Marshall, it is clear that Mrs. Marshall had expectancies of inheritance and/or gift that were realistic and substantial.

37. Debtor is informed and believes that Counterdefendant intentionally interfered with that expectancy by engaging in a concerted campaign to undermine Mrs. Marshall's rights and Mrs. Marshall's marriage to her Husband, by effectively imprisoning Mr. Marshall against his wishes, by surrounding Mr. Marshall with hired agents who reported to the Younger Son, by stationing armed guards to prevent access and personal contact between the Husband and Wife, by cutting off support and obstructing the expressed wishes of Mr. Marshall, by deceiving Mr. Marshall, by attempting to undo gifts made by Mr. Marshall, by preparing documents and by ostensibly making transfers of property of Mr. Marshall which were inconsistent with his expressed wishes and desires, by making misrepresentations against Mrs. Marshall, by cutting off income to Mr. and Mrs. Marshall, by cutting off payments to professionals retained to assist Mrs. Marshall, by suborning false testimony against Mrs. Marshall, by abusing legal process, and by other actions that shall be proven at trial. Mrs. Marshall is

informed and believes such interference was tortious, and marked by fraud, duress and undue influence.

38. As a proximate result of such interference, Debtor has been damaged in an amount to be proven at trial but which amount Debtor believes exceeds $300 million.

39. Mrs. Marshall is informed and believes that at all pertinent times the Counterdefendant has acted toward her in an outrageous, despicable, and vindictive manner, with personal hatred, malice and ill-will, in conscious disregard of Mrs. Marshall's rights, with an intentional purpose to injure, vex and annoy her, all for the Younger Son's financial gain, such that the Counterdefendant should pay punitive damages in an amount and of a magnitude similar to or greater than the financial gain seized by him.

* * *

OPPOSITION BRIEF

Supreme Court, U.S.
FILED
AUG 20 2010
OFFICE OF THE CLERK

No. 10-179

IN THE

Supreme Court of the United States

In re: VICKIE LYNN MARSHALL,
Debtor.

HOWARD K. STERN, EXECUTOR
OF THE ESTATE OF VICKIE LYNN MARSHALL,
Petitioner,

v.

ELAINE T. MARSHALL, EXECUTRIX
OF THE ESTATE OF E. PIERCE MARSHALL,
Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

Section 157(b)(1) of Title 28 confers jurisdiction on the bankruptcy courts to finally decide "core" proceedings that either "arise under" the Bankruptcy Code or "arise in" a case under the Code. 28 U.S.C. § 157(b)(1). For non-core matters that are "related to" a bankruptcy case, section 157(c) confers jurisdiction on a bankruptcy court to enter proposed findings of fact and conclusions of law, subject to *de novo* review in the district court (unless the litigants expressly agree otherwise as prescribed in Rule 7012(b) of the Federal Rules of Bankruptcy Procedure). 28 U.S.C. § 157(b)(1).

Applying the reasoning of this Court's landmark decision in *Katchen v. Landy*, and with due regard to this Court's decision in *Marathon*, the court below concluded that Petitioner's state law claim for "tortious interference with an expectancy of a gift" was not a "core" matter "arising in" a bankruptcy case "because [her tort claim was] not so closely related to [Respondent's] defamation claim that it must be resolved in order to determine the allowance or disallowance of his [defamation] claim against her bankruptcy estate." Pet. App. 51. In reaching this conclusion, the court below gave full meaning to the *complete* statutory text, not merely the portion Petitioner recites. Likewise, the decision below is fully consistent with settled bankruptcy

practice and does not conflict with the decisions of other courts of appeals to have addressed the issue, which decisions also follow *Katchen* and give due regard to *Marathon*.

In proper context, the questions presented are:

1. Whether the court below properly considered the complete statutory text in reaching its conclusion, not simply the incomplete portion Petitioner recites?

2. Whether, as the court below concluded, Congress has limited the jurisdiction of the bankruptcy courts to finally decide a state law counterclaim that is not inextricably intertwined with a claim?

3. Whether, consistent with the approach taken by every other court of appeals to have addressed the issue, the court below properly followed this Court's reasoning in *Katchen* and gave due regard to *Marathon* in applying the relevant statutory text?

4. Where, as here, the relevant rules of procedure require that consent to the final adjudication of a state law counterclaim in a bankruptcy court must be "express," has a creditor consented to have a bankruptcy court finally decide the counterclaim where the creditor vigor-

ously objected to the bankruptcy court's jurisdiction to adjudicate the counterclaim, moved the court to abstain, and sought to withdraw the litigation to another forum?

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PRELIMINARY STATEMENT

Petitioner, Howard K. Stern ("Stern"), is the executor of the estate of the late Vickie Lynn Marshall ("Vickie"), the former wife of the late J. Howard Marshall II ("J. Howard"). Respondent, Elaine T. Marshall ("Elaine"), is the executrix of the estate of the late E. Pierce Marshall ("Pierce"), J. Howard's son.

Vickie sued Pierce in Texas state court, alleging that he had "tortiously interfered" with her expectancy of receiving a gift from J. Howard. Following a five-and-a-half month jury trial, the Texas court rejected Vickie's claim, concluding in a final judgment that Vickie was entitled to take nothing from Pierce.

During the course of the state court action, Vickie filed for bankruptcy in California and pursued the same "tortious interference" claim against Pierce in the Bankruptcy Court. Pet. App. 13. The Bankruptcy Court determined that it had jurisdiction to finally resolve Vickie's "tortious interference" claim on the theory that the claim constituted a "core" bankruptcy matter asserted in response to a defamation claim that Pierce held against Vickie. Pet. App. 306-07. On appeal, the District Court reversed, concluding that Vickie's tort claim and Pierce's defamation claim were not sufficiently related to justify "core" adjudication in the Bankruptcy Court at the expense of Pierce's right to defend against

Vickie's claim in an Article III forum. Pet. App. 280-81, 283. On further appeal, the Ninth Circuit affirmed the District Court, holding similarly that Vickie's claim was not a "core" proceeding requiring administration in bankruptcy "because it [was] not so closely related to Pierce['s] defamation claim that it must be resolved in order to determine the allowance or disallowance of his claim against her bankruptcy estate." Pet. App. 51. In so holding, the court below upheld the District Court's vacatur of the Bankruptcy Court's non-Article III adjudication of Vickie's state law claim and permitted the Texas state court's comprehensive, five-and-a-half month jury trial adjudication to stand as the first final judgment resolving critical issues dispositive of her claim. (Stern does not seek further review of the court's preclusion determination.)

The decision of the Court of Appeals provides no occasion for certiorari review. First, there is no split of authority on the jurisdictional question. The decisions of the few courts of appeals to have addressed the issue are logically consistent with each other, and all follow the reasoning of this Court's decision in *Katchen v. Landy*. Second, in addition to following *Katchen*, the decision below does not conflict with this Court's other precedents and is also fully consistent with the governing statutory text and Congress' intent in crafting the current bankruptcy jurisdictional provisions. Third, the decision be-

low does not upset settled bankruptcy practice and has not generated confusion. On the contrary, it is consistent with settled practice.

Certiorari should also be denied because this case presents a poor vehicle to address the jurisdictional issue raised. To say the least, the facts of this controversy are atypical. Further, the Bankruptcy Court's assumption of jurisdiction encounters serious jurisdictional difficulties beyond those raised in the petition, as the concurrence below explained. These additional jurisdictional difficulties are by themselves fatal to the adjudication of Vickie's claim in the Bankruptcy Court.

The underlying litigation in this case is quickly approaching its third decade. All of the original litigants have passed away. The decision of the Court of Appeals fully and finally resolves the matter by permitting the results of a five-and-a-half month state court jury trial proceeding to control the outcome. In addition, the decision of the Court of Appeals likewise avoids litigation over a host of unresolved issues, including whether (1) Pierce was entitled to a jury trial in the federal proceeding, (2) Vickie's claim is barred by the Texas statute of frauds, (3) Pierce's due process rights were violated, (4) there is any evidence to support Vickie's claim that Pierce engaged in wrongdoing, and (5) the

other jurisdictional issues addressed by the concurrence. Certiorari should be denied.

STATEMENT

The relevant facts are hotly contested. The contest is heightened because the relevant state and federal courts reached diametrically opposed conclusions on the same factual issues. In addition, the record is all the more complicated because the decision of the Bankruptcy Court rests on "presumed" facts, whereas the decision of the state court rests on the results of a five-and-a-half month jury trial. Further, Stern mistakenly characterizes both the facts and the course of the state and federal proceedings. For the sake of brevity, Elaine corrects or qualifies only those mistakes that are particularly relevant.

Although Stern states at the outset that J. Howard "attempted to provide for Vickie through an inter vivos trust," and that Pierce "suppressed or destroyed the trust instrument," Pet. 2, these statements require qualification. It is true that the District and Bankruptcy Courts made "findings" adverse to Pierce on these points. As the Court of Appeals observed, however, "the district court made its factual findings without the benefit of the percipient witnesses that Pierce ... sought to have testify as part of his defense." Pet. App. 63 n.33. Likewise, the Bankruptcy Court made its findings on the basis of "deemed" facts and without allowing Pierce to put on his

case. *Marshall v. Marshall*, 392 F.3d 1118, 1126-27 (9th Cir. 2004). Moreover, when the Court of Appeals inquired directly (and insistently) of Stern's counsel whether there was any actual *evidence* in the record to back up the Bankruptcy and District Courts' adverse findings on these matters, Stern's counsel was unable to cite to any. Tr. 35-37 Oct. 9, 2003. Thus, although Stern's statements are based on the Bankruptcy and District Court's "findings," they remain highly disputed.

A. Background

J. Howard married Vickie, his third wife, in June of 1994, when J. Howard was eighty-nine and Vickie was twenty-six. ER-95, 2420.[1] Both prior to and during their marriage, J. Howard gave Vickie substantial gifts worth over $6 million. ER-2536-39, 2547-48. During his life, J. Howard stated repeatedly that he intended to provide for Vickie with the gifts that he gave her during his lifetime. ER-2417-18, 2498, 2509, 2959-61, 3404-05. In line with this intention, two weeks after he married Vickie, J. Howard executed his final amended and restated living trust instrument, irrevocably fixing the terms of his living trust in a manner that left the bulk of

[1] The term "ER" refers to certain "excerpts of record" filed in the Ninth Circuit.

his estate to Pierce. ER-645-46, 1018, 3210, 3264-68.

B. The Probate Court Proceedings

Stern contends incorrectly that Vickie "first appeared in [the Texas probate court] proceeding in 1998, when she joined a pending will contest." Pet. 4. As the Court of Appeals explained, in April *1995* (several months prior to J. Howard's death), Vickie commenced proceedings in the Texas probate court (the "Probate Court"), seeking a declaration concerning the validity of the living trust and alleging that Pierce had tortiously interfered with her property rights concerning J. Howard's assets. Pet. App. 11; ER-5615-17, 5620. Three days after J. Howard died, Vickie filed a further application in the Texas Probate Court, stating that J. Howard had died intestate. Pet. App. 11; ER-816-18. Pierce opposed this application and sought to admit his father's will. ER-836-45. Vickie thereafter contested the will in the Probate Court, challenged the validity of the estate plan, and pursued her claim against Pierce in the probate case (the "Probate Case"). ER-1319-31, 2863-65, 5523-31.

Stern contends incorrectly that Vickie only "prophylactically" filed her tortious interference claim in the Probate Court, asserting that Vickie did not intend to litigate her claim there or participate robustly in the Probate Case. Pet. 4. As the Court of Appeals explained, Vickie partici-

pated fully in the Probate Case, litigated her tortious interference claim there, and likewise litigated all of her allegations involving J. Howard's intent and Pierce's conduct. Pet. App. 61; *Marshall*, 392 F.3d at 1128-29.

In particular, prior to trial in the Probate Case, Vickie identified the causes of action against Pierce that she proposed to try to the Texas jury, including her claim of tortious interference with a gift, ER-4073, 4076-78, 4089, 4102, and later stressed to the jury that "[t]his is a case about tortious interference with an intent to give an *inter vivos* gift ...." ER-4068, 4106, 4134. Vickie called seven witnesses in the Probate Case. ER-4069-70. She called three additional witnesses in rebuttal. ER-4070-71. Vickie's counsel questioned at least fourteen other witnesses. ER-4070-71. Vickie herself testified in the Probate Court for approximately six days, including extensively regarding her alleged expectancy of a gift. ER-4071.

All told, the Probate Court heard the testimony of over forty witnesses and received hundreds of items of evidence. ER-4066-71, 4706-27. Following the jury's verdict, the Probate Court entered its judgment on August 15, 2001, disposing of all claims and issues related to J. Howard's intended disposition of his property, including Vickie's claim. ER-4001-22. On December 7, 2001, the Probate Court entered its second

amended final judgment (the "Probate Judgment"). ER-4706, 4727. The Probate Court admitted J. Howard's will to probate, finding the will and living trust to be genuine and valid and not the product of improper conduct. ER-4714-15, 4717.

The Probate Court specifically ruled that "[J. Howard] did not intend to give and did not give to [Vickie] a gift or bequest from the Estate of [J. Howard] or from the [living trust – which contained all of his assets] either prior to or upon his death" and "that [Vickie] does not possess any interest in and is not entitled to possession of any property within the Estate of [J. Howard] or any property [of the living trust] because of any representations, promises, or agreements." ER-4721. The Probate Court also held that (1) all of Vickie's claims were resolved and dismissed; (2) Vickie was entitled to "take nothing" from Pierce; and (3) Pierce was entitled to his inheritance free and clear of any claim by Vickie. ER-4718-19, 4721.

It is true that, during the course of the proceedings in the Probate Court, Vickie attempted to withdraw from the case by "nonsuiting" her claims. As the Court of Appeals explained, however, the Probate Court refused to let her withdraw. Pet. App. 20-21; *Marshall*, 392 F.3d at 1128. Stern contends incorrectly that, "[a]fter nonsuiting her claims, Vickie remained

in the probate proceedings only as a counterdefendant on a sanctions claim by Pierce." Pet. 4. As the Court of Appeals noted, Vickie remained as a defendant to Pierce's declaratory judgment action seeking a determination of Vickie's rights and Pierce's liabilities. Pet. App. 21 & n.19; ER-4713.[2]

As the Court of Appeals concluded, all of the issues regarding J. Howard's intent to give Vickie a gift and Pierce's alleged misconduct "were fully and fairly litigated by Vickie ... and Pierce ... in the Texas probate court." Pet. App. 61. Further, "[d]uring the five-month trial in Texas, the jury and judge considered the evidence and arguments advanced by the parties, and the Texas probate court issued a reasoned opinion based upon the findings of fact as made by the unanimous jury." Pet. App. 61.

C. The Defamation Case

During the pendency of the Probate Case, Vickie's lawyers made various defamatory allegations against Pierce. ER-930. Subsequently, Pierce commenced a defamation action in Texas

[2] Stern observes that the Bankruptcy Court enjoined Pierce from pursuing certain aspects of this litigation in the Probate Court. Pet. 5. The District Court, however, set aside the Bankruptcy Court's improper injunction. ER-3989.

state court against Vickie and two of her lawyers for these defamatory statements, alleging that Vickie was responsible for the conduct of her attorneys. SER-6001.[3] After Vickie commenced her bankruptcy case, Pierce dismissed her without prejudice from the defamation suit. Pet. App. 14 n.10.

D. The Bankruptcy Proceedings

On January 25, 1996, while the probate proceedings were ongoing and in the midst of the defamation suit, Vickie filed for bankruptcy in the United States Bankruptcy Court for the Central District of California. ER-2642. As a result of her bankruptcy filing, the defamation action against her was stayed, *see* 11 U.S.C. § 362, and, as noted, Pierce dismissed her "without prejudice" from the defamation action. Pet. App. 14 n.10.

On May 7, 1996, Pierce filed a complaint in the Bankruptcy Court seeking a determination that, in the event Vickie were found to be liable for defamation in state court, her liability would not be dischargeable in her bankruptcy proceeding. ER-922-32. In filing his complaint, Pierce did not request the Bankruptcy Court to deter-

[3] The term "SER" refers to certain "Supplemental Excerpts of Record" filed in the Ninth Circuit.

mine whether Vickie was, in fact, liable for defamation; he requested only a determination that whatever her liability might be, it was non-dischargeable. Pet. App. 67-68 (Kleinfeld, J., concurring); ER-922-26. Over a month later, on June 12, 1996, Pierce also filed a proof of claim, attaching the nondischargeability complaint. Pet. App. 67-68; SER-6020.

On June 14, 1996, Vickie filed a counterclaim against Pierce's nondischargeability complaint, alleging that J. Howard intended to give her a gift worth tens of millions of dollars and that Pierce had interfered. ER-936, 954. Vickie later objected to Pierce's proof of claim separately, but raised no counterclaim to Pierce's proof of claim. SER-6031-32.

Stern contends incorrectly that Pierce "brought his defamation claims into the bankruptcy court" and suggests that Pierce was content to litigate Vickie's claim in that forum. Pet. 2-3, 10 n.4. As the Court of Appeals explained, Pierce objected to the Bankruptcy Court's assertion of jurisdiction over Vickie's claim, requested that the Bankruptcy Court abstain, and also moved to have the litigation withdrawn to the District Court. *Marshall*, 392 F.3d at 1126; ER-957, 1049-69; SER-6754. As the District Court also concluded, Pierce did not consent to the Bankruptcy Court's jurisdiction. Pet. App. 266 & n.17; Fed. R. Bankr. P. 7012(b).

On March 5, 1999, while Vickie's counterclaim for tortious interference remained pending, Vickie confirmed her chapter 11 plan of reorganization. ER-2200-02. Pursuant to the Bankruptcy Court's confirmation order, Vickie was granted a discharge of her debts. ER-2201.

On November 5, 1999, the Bankruptcy Court granted Vickie's motion for summary judgment on Pierce's nondischargeability complaint. ER-2756-58. Instead of resolving the narrow bankruptcy question of nondischargeability, the court summarily determined that Vickie had no liability for any defamatory conduct. ER-2757. Following her bankruptcy discharge and the subsequent summary resolution of Pierce's underlying defamation claim, Vickie continued to litigate her tortious interference claim against Pierce in both the Bankruptcy Court and the Probate Court.

In the course of its five days of hearings on Vickie's counterclaim, the Bankruptcy Court severely circumscribed Pierce's presentation of evidence and made findings of fact adverse to him as a sanction for alleged discovery abuses that remain strenuously disputed. ER-2173-75, 2641-49. The Bankruptcy Court had previously entered its sanctions order against Pierce on February 2, 1999. As the Court of Appeals explained, "[t]he sanctions imposed by the court

deemed almost all facts alleged in the pleadings filed by the attorneys for Vickie ... to be admitted facts ...." *Marshall*, 392 F.3d at 1126. In addition, "[a]s a result of the sanctions order, [Pierce] was not allowed to present conflicting evidence ...." *Id.* at 1127; Pet. App. 19 n.17. Pierce appealed the sanctions order to the District Court. On March 9, 1999, the District Court vacated the sanctions order, finding that the order was not supported by the record. ER-2211-12, 5744-49. On remand, and without taking evidence, the Bankruptcy Court reimposed its sanctions order. ER-2240.

As the Court of Appeals explained, on January 18, 2000, "the bankruptcy court *sua sponte* withdrew its sanctions order, but did not change any of its other rulings which had been based on the allegations by Vickie ... deemed true." *Marshall*, 392 F.3d at 1127. As the Court further observed, the Bankruptcy Court "did not hold another evidentiary hearing." *Id.*

On September 27, 2000, nearly a year after it summarily resolved and dismissed Pierce's underlying defamation claim, the Bankruptcy Court issued a decision concluding that Vickie had an expectancy of an inheritance, based on a "widow's election" theory, and awarded Vickie $449,754,134. Pet. App. 18; ER-3031-38. On October 6, 2000, the Bankruptcy Court *sua sponte* issued a revised opinion, in which the court

abandoned its "widow's election" theory and deemed that Vickie had an expectancy of a substantial portion of J. Howard's wealth. Pet. App. 19; ER-3047-55. Concluding on the basis of presumed facts that Pierce interfered with this expectancy, the court again awarded Vickie $449,754,134. On November 21, 2000, the Bankruptcy Court assessed punitive damages against Pierce in the amount of $25 million, and on December 29, 2000, entered judgment in Vickie's favor for approximately $474 million (the "Bankruptcy Judgment"). ER-3360.

In its opinion of December 29, 2000, the Bankruptcy Court concluded that it had jurisdiction to enter the Bankruptcy Judgment, rejecting Pierce's argument that the "probate exception" to federal jurisdiction applied. Pet. App. 286-99. In addition, the court concluded that Vickie's claim for "tortious interference" constituted a counterclaim to Pierce's defamation claim and, thus, a "core" bankruptcy proceeding under 28 U.S.C. § 157(b)(2)(C). ER-306-07.

E. The District Court Proceedings

Pierce appealed the Bankruptcy Judgment to the United States District Court for the Central District of California. On June 20, 2001, the District Court affirmed the Bankruptcy Court's determination that the "probate exception" did not apply, but reversed the Bankruptcy Court's conclusion that Vickie's tortious interference

claim constituted a "core" proceeding that the Bankruptcy Court could finally resolve and vacated the Bankruptcy Judgment. Pet. App. 283. Stern contends that "the district court concluded that Vickie's claim was a *compulsory counterclaim* to Pierce's defamation claim." Pet. 6 (emphasis added). The District Court, however, did *not* determine that Vickie's claim was a "compulsory" counterclaim; the court consistently referred to it merely as a "counterclaim," stating that "it is not certain that Vickie's counterclaim arises from the same transaction as Pierce's proof of claim." Pet. App. 280. The District Court concluded that Vickie's claim was not "core" because it was only "somewhat related" to Pierce's defamation claim, and Pierce was entitled to an adjudication of Vickie's allegations in an Article III forum. Pet. App. 283.

Following vacatur of the Bankruptcy Court's decision, Pierce moved in the District Court to dismiss Vickie's "tortious interference" counterclaim on the grounds that it was barred by the doctrines of claim and issue preclusion following the Probate Court's final judgment. Pet. App. 222-23. The District Court denied the motion. Pet. App. 234.

Asserting its own bankruptcy jurisdiction, the District Court conducted a "de novo" review of Vickie's "tortious interference" claim. Like the Bankruptcy Court, the District Court refused to

hear many of Pierce's percipient witnesses, Pet. App. 63 n.33, but heard all of Vickie's witnesses. ER-5280-87. On March 7, 2002, the District Court ultimately awarded Vickie $88,585,534.66 on her claim (the "District Court Judgment"), concluding that J. Howard's signature on the Trust was forged; that the estate plan did not reflect J. Howard's true intentions; and that Pierce had thwarted J. Howard's intent to give Vickie an alleged gift by engaging in illegitimate "estate planning transactions for J. Howard," Pet. App. 90-214, 215-16, conclusions diametrically opposed to the determinations of the Probate Court and, Pierce argued, unsupported by any evidence.

In its ruling, the District Court did not reach the issue whether Pierce committed discovery abuse and declined to consider the Bankruptcy Court's sanctions rulings. Pet. App. 98-99. Prior to conducting its own hearings, the District Court ordered a complete "redo" of discovery that included turning over to Vickie's counsel not only all of the relevant documents but also all of Pierce's privileged communications with his attorneys. ER-4063. Pierce appealed the District Court Judgment to the Court of Appeals.

F. The Resolution of the Probate Exception Issue and the Decision Below

In vacating the District Court Judgment, the Ninth Circuit first held that the "probate exception" applied in this matter. *Marshall*, 392 F.3d at 1137. This Court subsequently reversed that determination. *Marshall v. Marshall*, 547 U.S. 293 (2006). Following this Court's remand, the principal parties passed away, and Stern, Vickie's former attorney, assumed responsibility for pursuing the interests of Vickie's estate as her executor. In addition, Elaine, Pierce's widow, assumed responsibility for pursuing the interests of Pierce's estate.

In the decision below, the Ninth Circuit held that Vickie's counterclaim to Pierce's non-dischargeability complaint was not a "core" bankruptcy proceeding arising in a bankruptcy case because her counterclaim was "not so closely related to Pierce Marshall's defamation claim that it must be resolved in order to determine the allowance or disallowance of his claim against her bankruptcy estate." Pet. App. 51. Accordingly, because it resolved a "non-core" matter, the Bankruptcy Judgment properly constituted merely *proposed* findings of fact and conclusions of law subject to "de novo" review in the District Court, and not a final judgment. *See* Fed. R. Bankr. P. 9033. In contrast, the Probate Judgment was properly a final judgment. Because the Probate Judgment preceded the Dis-

trict Court Judgment and resolved issues dispositive of Vickie's "tortious interference" claim, the Ninth Circuit applied the doctrine of issue preclusion and held that the earlier final Probate Judgment prevented Vickie from succeeding on her claim for tortious interference in the District Court. (Stern does not seek review of the court's preclusion determination.) Pet. App. 55-57.

In addition to the majority opinion, Judge Kleinfeld issued a concurring opinion in which he explained that he had "no quarrel with the majority opinion, and offer[ed] no argument against it" but instead wrote "merely to offer additional grounds that compel the same result." Pet. App. 66 (Kleinfeld, J., concurring). On May 5, 2010, the court below denied Stern's petition for panel rehearing and rehearing en banc.

REASONS FOR DENYING THE PETITION

Stern's petition for certiorari should be denied. There is no conflict among the courts of appeals on the jurisdictional question presented. The courts of appeals have held consistently that, if a creditor's claim against the debtor and the debtor's counterclaim against the creditor are inextricably intertwined such that the bankruptcy court cannot administer the claim without adjudicating the counterclaim, the adjudication of the counterclaim may be a "core" proceeding that the bankruptcy court may finally de-

termine. On the other hand, where (as here) the claim and counterclaim are not inextricably intertwined, the bankruptcy court may not finally adjudicate a state law counterclaim without the creditor's consent. The court below properly determined that Pierce's state law "defamation" claim was not inextricably intertwined with Vickie's state law "tortious interference" claim. This is entirely consistent with the approach taken by every other court of appeals to have addressed the same jurisdictional issue.

Likewise, the decision below comports fully with this Court's precedents, as well as the governing statutory text and Congress' intent in enacting the current provisions governing the exercise of bankruptcy jurisdiction. The current jurisdictional provisions were enacted in response to this Court's ruling in *Marathon*, and the decision below properly applied the relevant statutory provisions with due regard to relevant constitutional principles and congressional intent to circumscribe bankruptcy jurisdiction in cases of this kind to preserve a litigant's right to an Article III forum and jury trial adjudications of state law claims.

Contrary to Stern's contention, the decision below will not hamper the administration of bankruptcy cases. Nor has it generated confusion. Rather, the decision below follows and reinforces settled practice.

Further, this case presents a poor vehicle to address the questions presented. The facts are atypical, and, as Stern concedes, the issue arises only sporadically. Moreover, the Bankruptcy Court's assumption of jurisdiction in this case encounters crippling difficulties beyond those addressed in the petition. The petition should be denied.

A. The Decision Below Does Not Conflict with the Decisions of Other Courts of Appeals.

The decision below does not conflict with the decisions of other courts of appeals. Stern contends that the decision below "is the only circuit decision in the three decades since the statute's enactment to ever find a compulsory counterclaim to a proof of claim to be non-core." Pet. 21. Stern's argument attends to labels and ignores the relevant substance of this Court's analysis in *Katchen v. Landy*, and the actual holdings and analyses of the decisions of the courts of appeals that he cites.

1. The Decision Below Follows *Katchen*.

In *Katchen v. Landy*, the Court considered whether a bankruptcy court had "summary jurisdiction to order the surrender of voidable preferences [*i.e.*, certain payments a bankrupt debtor

makes to one creditor that prefer that creditor over others] asserted and proved by the trustee in response to a claim filed by the creditor who received the preferences." 382 U.S. 323, 325 (1966). The creditor in that case had filed proofs of claim asserting a particular debt, and the trustee responded with a counterclaim asserting that prior payments made to the creditor were voidable "preferences" that must be returned to the debtor. *Id.*

As a critical part of its analysis, the Court explained that section 57 of the Bankruptcy Act of 1898 – the relevant claims-allowance provision – contained an "important congressional directive around which much of this case turns. Subsection [57]g forbids the allowance of a claim when the creditor has 'received of acquired preferences ... void or voidable under this title' absent a surrender of any preference." *Id.* at 330 (quoting Bankruptcy Act of 1898 § 57(g)). In light of Section 57(g), the Court explained that "[u]navoidably *and by the very terms of the Act*, when a bankruptcy trustee presents a s 57, sub. g objection to a claim, *the claim can neither be allowed nor disallowed until the preference matter is adjudicated.*" *Id.* (emphasis added). Therefore, "in passing on a s 57, sub. g objection a bankruptcy court must necessarily determine the amount of the preference, if any, so as to ascertain whether the claimant, should he return the preference, has satisfied the condition im-

posed by s 57, sub. g on allowance of the claim." *Id.* at 334; *see also* 11 U.S.C. § 502(d). In other words, the Court concluded that it was essentially impossible to allow the claim without determining the preference counterclaim. The Court held that "examination of the structure and purpose of the Bankruptcy Act and the provisions dealing with allowance of claims therefore leads us to conclude, and we so hold, that the Act does confer summary jurisdiction to compel a claimant to surrender preferences that under s 57, sub. g. would require disallowance of the claim." *Id.* at 335.

The decision below adopted the same criteria for determining whether the Bankruptcy Court had "core" jurisdiction over Vickie's counterclaim. As the Ninth Circuit explained, "[c]ritical to the Court's decision [in *Katchen*] was the fact that the bankruptcy court was *unable to perform its statutory duty of allowing or disallowing the creditor's claim unless it ruled upon the trustee's counterclaim.*" Pet. App. 49 (emphasis added). In contrast, "the resolution of Vickie Lynn Marshall's counterclaim was not a necessary predicate to the bankruptcy court's decision to allow or disallow Pierce Marshall's defamation claim." Pet. App. 51. As the court explained, the "differences between the nature and scope of the factual allegations" in Pierce's underlying claim and Vickie's counterclaim demonstrated that Vickie's counterclaim "was not an

integral part of the claims allowance and disallowance process." Pet. App. 52. Noting that there was "little overlap of the legal elements of the claims at issue," the Ninth Circuit explained that "Pierce Marshall's defamation claim could be fully adjudicated without fully adjudicating Vickie Lynn Marshall's tortious interference claim." Pet. App. 54-55.

The factual record confirms that finding, as the Bankruptcy Court granted summary judgment for Vickie on Pierce's adversary complaint on November 5, 1999, but did not rule on Vickie's counterclaim *until nearly a year later* on September 27, 2000. Pet. App. 18. Further, although Vickie's claim for "tortious interference" involved her allegations concerning Pierce's conduct *prior* to J. Howard's death, Pierce's defamation claim against Vickie involved her conduct and statements *after* J. Howard died. Moreover, unlike the preference claim in *Katchen*, Vickie's "counterclaim" was not a federally created preference suit. The decision below is fully faithful to this Court's analysis in *Katchen*.

2. The Decision Below Is Consistent with the Decisions of the Other Courts of Appeals, Which Also Align with *Katchen*.

Stern contends erroneously that the decision below conflicts with the decisions of the Second Circuit in *Bankruptcy Servs., Inc. v. Ernst &*

Young, LLP (In re CBI Holding Co.), 529 F.3d 432 (2d Cir. 2008), the First Circuit in *Riley v. Decoulos (In re Am. Bridge Prods. Inc.)*, 599 F.3d 1 (1st Cir. 2010), the Fifth Circuit in *Bank of Lafayette v. Baudoin (In re Baudoin)*, 981 F.2d 736 (5th Cir. 1993), the Sixth Circuit in *United States v. McLeod Co. (In re McLeod Co.)*, No 90-3019, 1991 WL 96718 (6th Cir. 1991) (unpublished), and the Third Circuit in *Southeastern Sprinkler Co. v. Meyertech Corp. (In re Meyertech Corp.)*, 831 F.2d 410, 418 n.9 (3d Cir. 1987). None of these asserted "conflicts" are genuine, and Stern misapprehends the relevant rationale that unites these decisions: consistent with *Katchen*, whether it is necessary for the bankruptcy court to adjudicate a "counterclaim" in order to fulfill its administrative bankruptcy functions. Where it is, the courts have held the matter to be a "core" controversy that the bankruptcy court may finally resolve. Where it is not, as in this case, they have reached the opposite conclusion, consistent with the statutory text, relevant constitutional principles, and Congress' purpose in enacting the current jurisdictional scheme.

In *CBI*, a creditor filed a proof of claim seeking money for unpaid auditing and counseling services. 529 F.3d at 437. Following the creditor's filing of its claim, the disbursing agent under the debtor's plan of reorganization filed counterclaims against the auditor concerning

those very same professional services, alleging, *inter alia*, fraud, recklessness, and breach of fiduciary duty. *Id.* at 438, 441-42. Logically and legally, the creditor could not recover its fees if these allegations were meritorious. In this factual context, the Second Circuit considered whether the claims against the creditor were properly "core" proceedings under section 157(b) that the bankruptcy court could finally resolve. *Id.* at 459.

In finding the claim and counterclaim to be inextricably linked, the Second Circuit ultimately held that the counterclaims were core "because they are covered by the language of 28 U.S.C. § 157(b) *and are integrally related to the Proof of Claim.*" *Id.* at 438 (emphasis added). The Second Circuit reiterated a key point repeatedly throughout its decision that the claim and proof of claim were "factually and legally interconnected," and a determination on one "would likely be dispositive on the other." *Id.* at 438, 460, 462, 464.

Moreover, the Second Circuit in *CBI* expressly considered and *distinguished* the District Court decision in this case. *Id.* at 464. The Second Circuit explained that, whereas in *Marshall* there was merely an "attenuated" nexus between the transactions out of which Pierce and Vickie's claims arose, the claims in *CBI* were far more closely related, and, thus, "*Marshall's* context-

specific holding is inapposite here." *Id.* *CBI* simply does not establish a circuit split.

This reading of *CBI* is supported by an earlier Second Circuit decision in *Germain v. Connecticut Nat'l Bank.* 988 F.2d 1323 (2d Cir. 1993). In *Germain*, one of the litigants sought to interpret *Katchen* broadly and argued that, as soon as a proof of claim is filed, the claims allowance process is necessarily triggered for all counterclaims sufficient to permit the bankruptcy court to resolve them without a jury. *Id.* at 1327. In rejecting this argument, the Second Circuit explained that while it "agree[d] that the filing of a proof of claim is a *necessary* condition – the claims-allowance process can hardly begin before a claim is made – ... it is not a *sufficient* condition." *Id.* Distinguishing the facts in *Germain* from *Katchen*, the Second Circuit explained that "before a claim may be allowed, a court *must* resolve any preference issues that the trustee might raise." *Id.* In contrast, the state law counterclaims at issue in *Germain* did not have to be.

In *Am. Bridge*, a receiver appointed to administer the assets of American Bridge sought compensation for services he had rendered to the company. 599 F.3d at 3. Once the company was forced into bankruptcy, the receiver was obligated to account to the federal court as to the property he held as receiver. *Id.* The receiver

sought his compensation without filing an accounting. *Id.* Subsequently, the trustee of American Bridge's bankruptcy estate filed an adversary proceeding against the receiver for the receiver's actions in the capacity for which he sought compensation. *Id.* Accordingly, the claim and counterclaim, which both involved the work performed by the receiver, were inextricably related, also distinguishing *Am. Bridge* from this controversy.

In *Baudoin*, a creditor filed a proof of claim based on loans it had made to the debtor corporation. 981 F.2d at 741. Following the conclusion of its bankruptcy case, the debtor subsequently filed a lender liability suit based on an alleged "violation of these very same loan agreements." *Id.* While the *Baudoin* court stated in very general terms that a counterclaim to a proof of claim is a "core" proceeding under 157(b)(2)(C), the factual circumstances demonstrate that the "claim" and the "counterclaim" were inextricably linked. *Id.* at 741-42. Indeed, the Fifth Circuit explained that "[t]he contracts at issue are the *very loan agreements* which were the basis of the Bank's proof of claim in the prior bankruptcy. *It is difficult to imagine a more common nucleus of operative facts.*" *Id.* at 743 (emphasis added).

In *McLeod* (an unpublished opinion), a governmental agency sought the release of certain trucks the debtor was obligated to deliver

under contract. The debtor counterclaimed, seeking payment for the unpaid balance of the same contract. 1991 WL 96718, at *1. Obviously, the claim and counterclaim were inextricably linked, *id.* at *3, and the court concluded that the bankruptcy court had jurisdiction over the matter. Critically, the court did not hold that all compulsory counterclaims are necessarily "core." It simply held that the counterclaim in question was both compulsory and core. *Id.* at *4.

In *Meyertech*, a creditor filed a claim against the debtor for breach of contract. 831 F.2d at 412. The debtor counterclaimed, seeking the amount the creditor still owed under the same contract. *Id.* at 412-13. Once again, the claim and counterclaim were inextricably intertwined, and the court concluded that the counterclaim was a "core" matter that the bankruptcy court could finally resolve. *Id.* at 418.

Review of the circuit cases Stern cites reveals that each involves a contractual relationship between the relevant creditor and debtor and claims and counterclaims that are inextricably intertwined within that contractual relationship. None involve circumstances even remotely like those at issue here. Stern's contention that the decisions of the courts of appeals are in conflict rings hollow.

In addition to alleging a purported circuit split, Stern contends that the decision below "fundamentally changes bankruptcy law as applied for decades by bankruptcy and district courts." Pet. 24. Not so. Review of the cases Stern cites demonstrates that they also adhere to the dichotomy identified above: if the claim and counterclaim are inextricably intertwined such that one cannot be determined without the other, then the counterclaim may be a core matter that the bankruptcy court may finally resolve; if not, then not (absent the creditor's consent). Stern's characterization of the impact of the Court of Appeals' decision is simply inaccurate.

B. The Decision Below Properly Addresses *Marathon*.

Stern claims that the Ninth Circuit's analysis misapplies this Court's decision in *Marathon*. Pet. 32. It is Stern's analysis, however, that is in error. In *Marathon*, the Court invalidated the bankruptcy jurisdictional provisions that preceded the current scheme. In construing the current statutory text, it was entirely appropriate for the court below to consider the import of *Marathon* – just like every other Court of Appeals to have addressed the same issue.

A key point of *Marathon* was that a party should not be forced to litigate a state law claim in bankruptcy against his or her will without the benefit of an adjudication by an Article III judge

with the constitutional protections of life tenure and irreducible salary. *Northern Pipeline Constr. Co. v. Marathon Pipeline Co.*, 458 U.S. 50, 59-60 (1982); *id.* at 90-91 (Rehnquist, J., concurring in judgment). The decision below held correctly that Pierce should not be subjected to a non-Article III Bankruptcy Court determination at the expense of his right to a jury trial adjudication and the resolution of the matter in an Article III forum. Further, the decision below correctly recognized that *Marathon* places limits on what matters can be heard by non-Article III judges, and the decision below adheres to that teaching. Pet. App. 36-38, 46.

In *Marathon*, this Court considered whether Congress' grant of broad jurisdiction to bankruptcy judges in section 241(a) of the Bankruptcy Act of 1978 violated Article III of the United States Constitution. *Marathon*, 458 U.S. at 52. After the debtor in the case, Northern Pipeline, filed for bankruptcy, it sued one of its creditors, Marathon, for "alleged breaches of contract and warranty, as well as for alleged misrepresentation, coercion, and duress" – all state law claims. *Id.* at 56. Marathon sought to dismiss the suit "on the ground that the Act unconstitutionally conferred Art. III judicial power upon judges who lacked life tenure and protection against salary diminution." *Id.* at 56-57.

Agreeing with Marathon, the Court held that Congress could not grant non-Article III bankruptcy courts jurisdiction over Northern Pipeline's state law claims merely because they were "related to" the bankruptcy petition, because doing so "impermissibly removed most, if not all, of 'the essential attributes of the judicial power' from the Art. III district court." *Id.* at 87; *see also id.* at 91-92 (Rehnquist, J., concurring in judgment). The plurality of four Justices relied on the distinction between "public rights" matters, *i.e.*, arising "between the Government and persons subject to its authority," and "private rights" matters, *i.e.*, "the liability of one individual to another." *Id.* at 67-70. Justice Rehnquist's concurrence focused primarily on the narrower ground of the state law nature of the claim. *Id.* at 90-92. Because the concurrence constitutes a narrower, common ground with the plurality, its reasoning may be viewed as the holding of the Court. *See Marks v. United States*, 430 U.S. 188, 193 (1977).

Contrary to Stern's assertion, the fact that *Marathon* did not involve a compulsory counterclaim does not affect its application here. A key point of *Marathon* was that a person should not be forced to litigate a state law claim in bankruptcy against his or her will without the benefit of an Article III judge that has the constitutional protections of life tenure and irreducible salary. *Marathon*, 458 U.S. at 59-60; *id.* at 90-91

(Rehnquist, J., concurring in judgment). As in *Marathon*, Vickie sought to subject Pierce, despite his objection, to her purported state law cause of action without the benefit of the Article III adjudication to which he was entitled. *Id.* at 91. When Vickie asserted her tortious interference counterclaim in response to Pierce's complaint to determine the dischargeability of his claim for defamation, Pierce promptly objected to the adjudication of her claim in the non-Article III Bankruptcy Court. ER-957.

While this Court acknowledged in *Marathon* that Congress has substantial discretion to assign the adjudication of rights it creates (*e.g.*, preference actions) to whatever type of forum it desires, there is no comparable justification when the cause of action is not one of congressional creation. 458 U.S. at 83-84. Vickie's counterclaim is purely a creature of Texas law. ER-936. Accordingly, a non-Article III court could not constitutionally exercise jurisdiction over Vickie's claim in order to resolve it by final judgment.

C. The Decision Below Follows Congress' Intent.

Stern contends that the decision below runs afoul of Congress' intent in enacting section 157 and would effectively nullify part of the legislation. Once again, Stern is mistaken, and it is

his interpretation that would render part of the statute superfluous.

Following *Marathon*, Congress' primary concern in 1984 in enacting the current jurisdictional provisions was to pass a constitutional statute. *See, e.g.*, 130 Cong. Rec. H7493-7494 (daily ed. June 29, 1984) (Rep. Glickman) ("The conference report ... is intended to bring [the bankruptcy courts] into constitutional conformity ...."). Although it is true that some influential legislators stated that 95% of the cases would be core proceedings that a bankruptcy court may finally resolve, the legislation itself by its terms recognizes that significant matters are excluded. For example, sections 157(b)(2)(B), (O), and (b)(5) all provide for the explicit exclusion of personal injury torts from the scope of "core" proceedings that a bankruptcy court may finally resolve.

Stern argues that references to the legislative history support his theory, but his citations actually cut against him. For example, he quotes the comment of one legislator who stated his understanding that *Marathon* "was concerned only with State law issues that did not arise in the core bankruptcy function of adjusting debtor-creditor rights." Pet. 17 (citing 130 Cong. Rec. 6242 (daily ed. March 21, 1984) (Rep. Kindness)). Vickie's claim, however, is precisely such a state law issue: one that does not arise in the context of a "core bankruptcy function of adjusting

debtor-creditor rights" because it was not necessary to adjudicate her claim in order to administer her bankruptcy estate (any more than it was necessary to adjudicate the debtor's state law breach of contract claim in *Marathon*).

Stern states that, "[i]n accordance with its view of *Marathon*, Congress broadly defined core proceedings as those 'arising under' the bankruptcy code and 'arising in' bankruptcy cases." Pet. 17. But even a cursory glance at the statute reveals this characterization to be a glaring error as the statute says and does no such thing. As the Court of Appeals observed, the definitional provision of section 157(b)(2) defines the term "core proceeding" to include a non-exhaustive list of matters. Pet. App. 38 & n.24. The statute, however, does not define the phrases "arising under" or "arising in" set forth in section 157(b)(1), let alone define them to be synonymous with "core proceedings." Pet. App. 40-41. As the Court of Appeals correctly noted, the phrases "core" and "arising in" and "arising under" are distinct, and under section 157(b)(1), it is not enough for a matter to be a "core" proceeding in order to be finally resolved by a bankruptcy court. By its express terms, section 157(b)(1) requires that the matter must be a core proceeding (defined in section 157(b)(2)) and must also either "arise under" the Bankruptcy Code or "arise in" a case under the Code (not de-

fined). Pet. App. 37, 43. Stern's contrary characterization ignores half the statutory text.

Stern argues similarly that the decision of the court below "nullifies" section 157(b)(2)(C). Pet. 20. Stern's theory appears to be that section 157(b)(2)(C) defines "core" matters to include counterclaims against creditors who file proofs of claim, and this by itself is sufficient for jurisdiction purposes. As noted, however, the fatal problem with this theory is that Stern's interpretation eviscerates the additional requirement of section 157(b)(1) that the matter must also be "arising under" or "arising in" in order for a bankruptcy court to finally resolve it. Contrary to Stern's unfounded criticism, the decision below gives meaning to the entire statutory provision.

As the court below properly recognized (and like every other court of appeals to have addressed the issue), it is imperative in construing Section 157(b) to keep in view the constitutional concerns and restrictions articulated in *Marathon* that Congress hoped to avoid with the current statutory scheme. These include preserving the rights of creditors such as Pierce to Article III court adjudications and jury trials. The decision below is fully consistent with these important values.

D. The Decision Below Does Not Conflict with Other Precedents of this Court.

Stern contends that the Ninth Circuit's decision in this case is inconsistent with certain of the Court's post-*Marathon* decisions. Pet. 33-38. Stern is again mistaken.

In *Commodity Futures Trading Comm'n v. Schor*, this Court considered whether the Commodity Futures Trading Commission ("CFTC") could entertain state law counterclaims without violating Article III. 478 U.S. 833, 835-36 (1986). The dispute in that case arose after Schor initiated a CFTC reparations proceeding and filed complaints with the CFTC against ContiCommodity Services, Inc. ("Conti"). *Id.* at 837.

Schor's complaints to the CFTC alleged that Conti had caused Schor to have a debit balance in his trading account in violation of the Commodity Exchange Act ("CEA"). *Id.* Before it received notice of the reparations proceeding, Conti filed a diversity action in federal district court to recover the same debit balance owed by Schor. *Id.* Schor subsequently counterclaimed in the district court action, "reiterating his charges that the debit balance was due to Conti's violations of the CEA." *Id.* at 837-38. Additionally, Schor moved "on two separate occasions to dismiss or stay the District Court action" and argued that the CFTC reparations action would fully resolve and adjudicate all of the rights of

the parties in the district court action. *Id.* at 838. Acquiescing, Conti voluntarily dismissed the federal court action and "presented its debit balance claim by way of a counterclaim in the CFTC reparations proceeding." *Id.* After the Administrative Law Judge presiding over the reparations proceeding ruled in Conti's favor on both Schor's claims and Conti's counterclaims, "Schor for the first time challenged the CFTC's statutory authority to adjudicate Conti's counterclaim." *Id.*

This Court ultimately held that the jurisdictional grant was constitutional because "[t]he CFTC adjudication of common law counterclaims is incidental to, *and completely dependent upon*, adjudication of reparations claims created by federal law." *Id.* at 856 (emphasis added). The Court stressed that the constitutionality of the adjudicatory scheme at play in *Commodity Futures* was predicated on the fact that the jurisdiction at issue extended only to a "particularized area of law" and a "narrow class of common law claims," unlike the broader jurisdictional grant invalidated in *Marathon*. *Id.* at 852, 854-56. The Court further noted that the absence of consent in *Marathon* was a significant factor in determining that Article III forbade adjudication. *Id.* at 849; *see also Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33, 59 n.14 (1989) (explaining that the notion of waiver in *Commodity Futures* is "unavailable in the context of bankruptcy pro-

ceedings, because creditors lack an alternative forum to the bankruptcy court in which to pursue their claims."). The Court explained that "Schor expressly demanded that Conti proceed on its counterclaim in the reparations proceeding rather than before the District Court ... and was content to have the entire dispute settled in the forum he had selected until the ALJ ruled against him on all counts." *Commodity Futures*, 478 U.S. at 849.

Unlike the litigant in *Commodity Futures*, Pierce did not demand that Vickie's "tortious interference" claim be adjudicated in the Bankruptcy Court and never consented to its adjudication there. Further, it was not necessary to resolve Vickie's claim in order to allow or disallow Pierce's proof of claim, or to vindicate Congressional regulation of a "particularized area of law." (Congress has not purported to regulate "tortious interference" claims involving alleged gifts.) The facts of the two cases are thus entirely dissimilar, and the decision below comports with *Commodity Futures*.

Stern's reference to language from *Thomas v. Union Carbide Agric. Prods. Co.*, 473 U.S. 568 (1985), also does not advance his cause. Pet. 33. As *Thomas* stated, "practical attention to substance rather than doctrinaire reliance on formal categories should inform application of Article III." 473 U.S. at 587. In this case, the court be-

low adhered fully to "practical attention to substance"; it is Stern who champions formalistic labels.

Stern's reference to *Granfinanciera* and *Langencamp v. Culp*, 498 U.S. 42 (1990), are equally unavailing. Pet. 37. Both cases involved the effect of the filing of a proof of claim on a creditor's right to a jury trial with respect to *federal* bankruptcy causes of action asserted against the creditor, not state law counterclaims. *See Langencamp*, 498 U.S. at 43; *Granfinanciera*, 492 U.S. at 36-37. Under the governing statutory scheme, it is not possible to allow a proof of claim without resolving *federal* bankruptcy causes of action. 11 U.S.C. § 502(d). Not so with respect to a state law counterclaim of the kind at issue here. The decision below does not conflict with these precedents.

E. The Decision Below Addresses an Arcane Issue and Has Not Generated Confusion.

Stern contends that certiorari should be granted because "[t]he issues presented by this petition rarely reach the circuit level." Pet. 38. Contrary to Stern's explanation, however, that is because, over the past several decades, courts have settled on a consistent methodology in resolving the dispute – one of evaluating whether the claim and counterclaim are so intertwined that it is necessary for the bankruptcy court to

adjudicate the counterclaim in order to fulfill its administrative bankruptcy functions. Further, the fact that the issue arises so rarely counsels *against* granting certiorari – particularly where, as here, there is no need to correct any disagreement among the courts of appeals.

Moreover, Stern's argument that certiorari is warranted because "the nature of bankruptcy cases tends to discourage appellate review" is overstated because the same could be said of virtually any petition involving a bankruptcy matter. In addition, contrary to Stern's assertion, the reason why bankruptcy cases generate relatively few appeals as compared to general civil matters is that the vast majority of bankruptcy cases do not generate litigation, but are handled routinely in an administrative fashion.

Further, Stern's assertion that the decision below is "an outlier decision in an extraordinary case that alters long-standing practices" is both untrue and self-defeating. Pet. 39. The only thing true about this statement is that the case is indeed "extraordinary," but its arcane nature counsels *against* certiorari review, not for it.

Stern contends erroneously that the decision below "is already causing confusion." Pet. 39. For this, he cites only one decision that postdates the opinion below. *In re Gorilla Cos.*, 429 B.R. 308 (Bankr. D. Ariz. 2010). In *Gorilla*, how-

ever, a creditor filed a proof of claim asserting an unpaid balance owing on a promissory note, and the debtor counterclaimed, alleging that no amount was owed due to the creditor's fraud. The claim and counterclaim were thus inextricably intertwined and, therefore, "so unlike that in *Marshall*." *Id.* at 314. There is no reason for certiorari review.

F. This Case Presents a Poor Vehicle for Review of the Jurisdictional Issue.

Apart from the questions presented, there are numerous additional grounds why the Bankruptcy Court's assumption of jurisdiction was defective. These are examined by Judge Kleinfeld in his concurrence and would be properly reviewable in this Court because each was raised below. *See Granfinanciera*, 492 U.S. at 38-39 ("[W]ithout cross-petitioning for certiorari, a prevailing party may, of course, 'defend its judgment on any ground properly raised below whether or not that ground was relied upon, rejected, or even considered by the District Court or the Court of Appeals.'").

For example, as the concurrence explained, "[t]here is yet another independent reason, elementary and compelling even without the others, that the bankruptcy court was without jurisdiction over Vickie's counterclaim." Pet. App. 74 (Kleinfeld, J., concurring). Even if Pierce had asked the Bankruptcy Court to adjudicate his

defamation claim (which he did not), the Bankruptcy Court lacked jurisdiction to do so as his claim constituted a state law claim for personal injury, which cannot be a "core" matter that the Bankruptcy Court may finally resolve. Section 157(b)(5) of the Bankruptcy Code directs that "the district court shall order that personal injury tort and wrongful death claims shall be tried in the district court." 28 U.S.C. § 157(b)(5).

A defamation claim is properly a personal injury tort claim within the meaning of the statute. *See, e.g., Rizzo v Passialis (In re Passialis)*, 292 B.R. 346, 352-53 (Bankr. N.D. Ill. 2003) (bankruptcy court lacked jurisdiction under section 157(b)(5) to determine slander claim underlying dischargeability complaint); *see also Control Ctr., LLC v. Lauer*, 288 B.R. 269, 279 (M.D. Fla. 2002)). This is confirmed by reference to Texas law, which also characterizes a defamation suit as a personal injury action. *See In re Dillard Dep't Stores, Inc.*, 186 S.W.3d 514, 516 (Tex. 2006) (employee's defamation claim fell within the scope of an arbitration agreement that applied to "personal injuries"); *Brewster v. Baker*, 139 S.W.2d 643, 645 (Tex. Civ. App. 1940). Additionally, when Pierce filed his proof of claim attaching the non-dischargeability complaint, he checked the personal injury tort box on the form. Pet. App. 78; SER-6020.

Further, Vickie's "tortious interference" claim, is also a personal injury claim and, accordingly, was also required to be heard in the District Court. Moreover, even if Vickie's claim were not a personal injury tort, it would still be required to be adjudicated in the District Court because Pierce's defamation claim clearly is. As the Seventh Circuit explained in *Pettibone Corp. v. Easley*, bankruptcy judges "cannot try selected defenses in these tort cases .... The whole case, including defenses of all kinds, goes off to the district judge or the state court." 935 F.2d 120, 123 (7th Cir. 1991). Accordingly, as Elaine argued below and Judge Kleinfeld agreed, "[b]ecause Vickie's counterclaim was a personal injury claim, be it in defense of Pierce's defamation claim or an independent cause of action, the bankruptcy court would have lacked jurisdiction to enter final judgment on it." Pet. App. 75-76 (Kleinfeld, J., concurring). Section 157(b)(5) therefore presents yet another independent basis for the decision below and another compelling reason for this Court to deny the petition for certiorari.

There are numerous other grounds (summarized above) by which the Ninth Circuit could have reached the same result it reached below. *See* Pet. App. 65. Rather than address these issues, the Court of Appeals properly determined that the results of a comprehensive five-and-a-

half month jury trial should control the outcome of this controversy. Certiorari should be denied.

CONCLUSION

For the foregoing reasons, the Court should deny Stern's petition for a writ of certiorari.

Respectfully submitted,

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REPLY BRIEF

No. 10-179

Supreme Court, U.S.
FILED
AUG 31 2010
OFFICE OF THE CLERK

In The
Supreme Court of the United States

HOWARD K. STERN, EXECUTOR OF
THE ESTATE OF VICKIE LYNN MARSHALL,

Petitioner,

v.

ELAINE T. MARSHALL, EXECUTRIX OF
THE ESTATE OF E. PIERCE MARSHALL,

Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

PETITIONER'S REPLY IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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PETITIONER'S REPLY

This case presents a clear, clean, vitally important issue for review – is the Ninth Circuit correct that 28 U.S.C. §157(b)(2)(C) violates Article III of the Constitution by investing bankruptcy courts with core jurisdiction over all compulsory counterclaims to creditors' proofs of claim? As the leading bankruptcy treatise recognizes, this issue has been brewing since *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982) and its much-discussed footnote 31. *See* 1 Alan N. Resnick & Henry J. Sommer, Collier on Bankruptcy (16th ed. 2010) 3-32 to 3-34, ¶ 3.02[3][d][I].

While the bulk of this reply answers Pierce's legal arguments, his opposition brief also presents a highly misleading factual summary intended to dilute the candidacy of this case for certiorari; in particular, he portrays Vickie as forum-shopping her tortious interference claim, dragging Pierce into a federal forum he did not choose. Opp'n 1-2, 6-18. These distortions continue the win-at-any-cost litigation style that Pierce and his attorneys have pursued in this case at every level. The bankruptcy court called them on it,[1] as did the district court.[2] This Court saw

[1] The bankruptcy court found some of Pierce's counsel's representations to be "directly opposite" to the truth, *In re Marshall*, 273 B.R. 822, 832 (Bankr. C.D. Cal. 2002), and it imposed issue sanctions because of Pierce's "massive discovery abuse" (App. 320-26).

[2] The district court characterized some of Pierce's litigation tactics as "the height of bad faith" (App. 148-49 n.21), noted that

(Continued on following page)

through it, too.[3] There is insufficient space to correct all the distortions, but we briefly set the record straight regarding the most significant one.

As even the Ninth Circuit now recognizes, Pierce deliberately moved his pending state court defamation claim into the bankruptcy court, requiring Vickie to file her tortious interference compulsory counterclaim in response or lose it forever. App. 13-17. The suggestion that Vickie chose the federal forum to litigate against Pierce is a canard.[4]

if the evidence of the trust for Vickie had been insufficient "the discovery abuses in this case might have led the Court to deem this fact as established" (App. 137 n.17), and "encourage[d]" the Justice Department to investigate Pierce's chief witness, Edwin Hunter, for perjury prosecution (App. 160 n.28).

[3] When this case was previously before this Court, at oral argument Justice Stevens raised the fact that Pierce's brief contained a highly misleading quotation. *Marshall v. Marshall*, No. 04-1544, Tr. 51-52, Feb. 28, 2006. Two terms later, Justice Kennedy adverted to Pierce's counsel's tactics in the *Marshall* case during his argument of another case, stating, "And if you have repeated statements in your brief that require qualifications, if in your former argument in Marshal [sic], the Court is concerned with the accuracy of one of your citations, shouldn't we view with some skepticism what you tell us?" *Preston v. Ferrer*, No. 06-1463, Tr. 51, Jan. 14, 2008; *see also* Tr. 47-50.

[4] The opposition brief asserts that the petition "contends incorrectly that Vickie 'first appeared in [the Texas probate court] proceeding in 1998, when she joined a pending will contest,'" because in 1995 "Vickie commenced proceedings in the Texas probate court (the "Probate Court"), seeking a declaration concerning the validity of the living trust and alleging that Pierce had tortiously interfered with her property rights concerning J. Howard's assets." Opp'n 6.

(Continued on following page)

Having thus distorted the facts, the opposition brief then obfuscates the law, straining to make it appear as if the Ninth Circuit's newly-minted interpretation of §157(b)(2)(C) is simply business as usual, when in fact the Ninth Circuit radically departed from the uniform practice in the federal courts of treating all compulsory counterclaims as core by holding that core jurisdiction can constitutionally exist only in the rare circumstance that the resolution of the counterclaim is a "necessary precursor" to the allowance or disallowance of the claim itself.

The scores of bankruptcy court decisions the petition cites (Pet. 25-27) show this is an issue bankruptcy courts deal with every day. Yet because so few bankruptcy cases reach the circuit courts, the issue may fester for many more years unless the Court seizes this opportunity to confront it.

The bracketed words Pierce interpolates above wholly change what the petition actually stated, which was, "A Texas probate court *began administering Howard's estate* in August 1995 [citation] [and] Vickie first appeared in *that proceeding* in 1998, when she joined a pending will contest." Pet. 4 (emphases added). The earlier 1995 probate court proceeding was a *guardianship* proceeding initiated by *Pierce* to declare Howard incapacitated in which Vickie claimed Pierce was interfering with *Texas statutory spousal support* and which terminated when Howard died. Excerpts of Record ("ER") 724-37; Supplemental Excerpts of Record ("SER") 7959, 8005-06, 10194, 12595-96.

I. THE NINTH CIRCUIT'S NEW RULE DEPARTS SHARPLY FROM SETTLED LAW.

A. The Opinion Creates A Circuit Split.

Commentators have recognized that the opinion below "is a game-changing decision." Kevin M. Baum, *Ninth Circuit Holds That A Debtor's Compulsory Counterclaims Can Be "Non-Core,"* Am. Bankr. Inst. J. 48, 48 (July/Aug. 2010). It decisively "changed the law." *In re Gorilla Cos.*, 429 B.R. 308, 310 (Bankr. D. Ariz. 2010).

Undaunted, Pierce argues the Ninth Circuit's rule is nothing new because all other appellate courts holding compulsory counterclaims core "follow the reasoning of this Court's decision in *Katchen v. Landy* [, 382 U.S. 323 (1966)]." Opp'n 2. Nonsense. Only one of the five circuit decisions (Pet. 22-23), even mentions *Katchen* and it does so only on an irrelevant vacatur issue. *See In re CBI Holding Co.*, 529 F.3d 432, 459-65 (2d Cir. 2008) (core jurisdiction analysis); *id.* at 438, 466-69 (references to *Katchen*). Far from following the other circuits' cases, the Ninth Circuit cites none of them.

To make the opinion sound like business as usual, Pierce recharacterizes its holding that the resolution of the counterclaim must be a "necessary precursor" to resolving the creditor's claim (*see* App. 4) as meaning simply that the claim and counterclaim must be "inextricably intertwined"; he then points to similar language in *CBI*, 529 F.3d at 438 ("integrally related to the Proof of Claim") and *In re Baudoin*, 981

F.2d 736, 743 (5th Cir. 1993) ("common nucleus of operative facts"). Opp'n 18-19, 25, 27-28. But a compulsory counterclaim by definition is "integrally related" and "inextricably intertwined" with the proof of claim. Fed. R. Bankr. P. 7013; Fed R. Civ. P. 13(a); *In re Yagow*, 53 B.R. 737, 740 (Bankr. D.N.D. 1985) ("[a] counterclaim, compulsory in nature, is the type of counterclaim which would be considered integral"); *In re Beugen*, 81 B.R. 994, 1000 (Bankr. N.D. Cal. 1988) ("[a] compulsory counterclaim against a creditor that has asserted a claim is closely connected to the central bankruptcy function of determining claims").

Under the Ninth Circuit's "necessary precursor" standard, as opposed to Pierce's re-write, the counterclaims in the other circuit cases all would be non-core because each entails factual and legal elements beyond what would be required to prove or disprove the proof of claim. *See* Pet. 22-23.

In *CBI*, for example, the debtor counterclaimed for $70 million in damages for accounting malpractice committed from 1992 through 1994 in response to an auditor's proof of claim for an unpaid 1994 audit; the Second Circuit held the counterclaims were core, even though the proof entailed factual elements far beyond what would have been necessary to resolve the proof of claim. 529 F.3d at 439-42, 461 & n.12. Significantly, the court held another set of counterclaims core although "none of them affect the allowance of [the auditor's] fees claim against the estate," because they "are related to and arise out of the same transaction as [the auditor's] fee claim, and a determination on

[those counterclaims] would likely be dispositive of [the auditor's] claim." *Id.* at 464.[5]

Similarly, *In re American Bridge Products*, 599 F.3d 1, 4 (1st Cir. 2010) involved a receiver's proof of claim seeking compensation for services; the debtor's compulsory counterclaims addressed not only the value of those services but also "losses to the estate caused by negligence and/or breach of fiduciary duty." *In re Am. Bridge Prods.*, 398 B.R. 724, 730 (D. Mass. 2009). Even though the tort claims required proof beyond mere allowance/disallowance of the receiver's compensation claim, the First Circuit held the counterclaims core, broadly pronouncing that "a compulsory counterclaim appears to fall within the statutory definition of core proceedings." 599 F.3d at 4.

The opinion below is the only circuit case ever to hold a compulsory counterclaim non-core, and it finds Vickie's counterclaim non-core even though its successful resolution establishes the affirmative defense of truth to Pierce's defamation claim. A compulsory counterclaim will rarely "essentially merge" (*see* App. 4) with the creditor's claim in terms of proof; otherwise it would merely constitute an affirmative defense. Under the Ninth Circuit's new test, few counterclaims would be core other than "avoiding

[5] Although Pierce claims *Germain v. Connecticut National Bank*, 988 F.3d 1323 (2d Cir. 1993) supports his "reading of *CBI*" (Opp'n 26), *CBI* itself distinguishes *Germain*, noting the debtor's claims "were not asserted to counter the proof of claim" and the debtor never objected to the proof of claim. *CBI*, 529 F.3d at 467.

power" counterclaims, such as the preference counterclaim in *Katchen*, since only those would be necessary precursors to resolving the proof of claim.

B. Pierce Ignores The Legion Of Contrary Bankruptcy And District Court Authority.

Pierce argues that, "as Stern concedes, the issue [raised in the petition] arises only sporadically." Opp'n 20. But the petition explains that these issues rarely reach *the circuit level*, given the nature and economics of bankruptcy cases. Pet. 38-39. Issues involving compulsory counterclaims to proofs of claim occur frequently in bankruptcy, as the trial court decisions cited at pages 24-27 of the petition show.

Pierce is wrong that these cases all follow the Ninth Circuit's new rule. Opp'n 29. Rather, the bankruptcy and district courts (other than in a few outdated cases, *see* Pet. 28-29) uniformly have treated as core *all* compulsory counterclaims, i.e., those arising from the same transaction as the proof of claim. *See, e.g.*, *In re Geneva Steel, LLC*, 343 B.R. 273, 278 (Bankr. D. Utah 2006) (creditors "may not claim against the estate without subjecting themselves to compulsory counterclaims attaching to their claims"); *In re Asousa P'ship*, 276 B.R. 55, 67 (Bankr. E.D. Pa. 2002) ("a creditor who files a claim in the bankruptcy court in this circuit impliedly consents to being sued on counterclaims arising out of the same but not unrelated transactions"); *In re Iridium Operating*, 285 B.R. 822, 832 (S.D.N.Y. 2002) ("non-core claims

against a creditor in an adversary proceeding will be considered core" where "the claim arises out of the same transaction as the creditor's proofs of claim or setoff claim"); *In re Lion Country Safari, Inc.*, 124 B.R. 566, 569 (Bankr. C.D. Cal. 1991) ("a debtor's counterclaim arising from the same transaction as the creditor's claim against the estate may be decided in the same manner as the claim").

II. PIERCE'S MISCONSTRUCTION OF §157(b) IS NO BASIS FOR DENYING CERTIORARI.

Pierce insists the Opinion "is fully consistent with the governing statutory text and Congress' intent in crafting the current bankruptcy jurisdictional provisions." Opp'n 2. But his argument rests on an insupportable reading of the statute.

Faced with the reality that Congress expressly included counterclaims to proofs of claim in its non-exhaustive list of proceedings that Congress designated as "core," Pierce argues that §157(b)'s language authorizes bankruptcy courts to enter final judgment only if the proceeding is *both* "core" *and also* "arises under" the bankruptcy code or "arises in" the bankruptcy case. Opp'n 34-35. However, the statute demonstrates that Congress divided proceedings into two categories: "core" proceedings (i.e., claims that fall within the "arise under" and "arise in" definitions), which the bankruptcy court can finally decide, and proceedings merely "related to" the bankruptcy

case, which the district court must finally decide. For example,

- §157(b)(3) specifies bankruptcy judges shall determine "whether a proceeding is a core proceeding under this subsection or is a proceeding that is otherwise related to a case under title 11" and a determination that "a proceeding is not a core proceeding shall not be made solely on the basis that its resolution may be affected by State law";
- §157(c)(1) specifies that bankruptcy judges "may hear a proceeding that is not a core proceeding but that is otherwise related to a case under title 11" but "[i]n such proceeding" can only submit proposed findings.

If Congress had intended Pierce's construction, it would have required bankruptcy courts to determine whether a proceeding is "a core proceeding" *and* whether it "arises under" or "arises in," and it would have similarly qualified all other "core" references.

III. CERTIORARI IS NECESSARY BECAUSE THE CIRCUIT SPLIT ARISES FROM DIFFERING INTERPRETATIONS OF THIS COURT'S PRECEDENT.

Pierce attempts to validate the opinion by claiming it simply applies this Court's precedent. *See* Opp'n 20-22, 29-32, 36-39. But that is exactly why certiorari is necessary. This Court has *never* addressed the

constitutionality of §157(b)(2)(C), and courts have reached differing conclusions on the application of this Court's existing precedent to that statute. *See* Pet. 29-38. Absent certiorari, the issue will remain unsettled.

For example, in attempting to transform *Katchen* into an Article III case that imposes limitations on compulsory counterclaim adjudication, Pierce (like the Ninth Circuit) ignores that:

- *Katchen* did not consider Article III and only *construed* the 1898 Bankruptcy Act. *Marathon*, 458 U.S. at 79 n.31.
- The 1898 Act had no provision authorizing bankruptcy courts to decide counterclaims and, until this Court considers §157(b)(2)(C), the power of bankruptcy courts to enter final judgment on counterclaims will remain unsettled. 1 Collier on Bankruptcy, *supra*, at 3-32 to 3-34, ¶ 3.02[3][d]; Pet. 30-32.
- Even after *Katchen*, courts applying the 1898 Act recognized that bankruptcy courts had summary jurisdiction over compulsory counterclaims (Pet. 14-15).
- This Court itself has construed *Katchen* as supporting a bankruptcy court's entry of final judgment on state-law counterclaims to a proof of claim that "arose out of the same transaction." *Commodity Futures Trading Comm'n v. Schor*, 478 U.S. 833, 852 (1989).

IV. THIS CASE IS AN APPROPRIATE VEHICLE FOR CERTIORARI NOTWITHSTANDING STATEMENTS IN THE CONCURRENCE.

Pierce argues that this case is a poor vehicle for reviewing the issues raised in the Petition because the concurrence purportedly provides additional reasons Vickie's counterclaim might be non-core. Opp'n 41-44. But he ignores that the concurrence rests on factual assertions the majority rejected and the record refutes. Pet. 10-11 n.4. Moreover, even if the circuit court might address additional issues on remand, that is no reason to deny certiorari. *See Marshall v. Marshall*, 547 U.S. 293 (2006) (review of probate-exception ruling granted, even though Ninth Circuit had not addressed other potentially dispositive arguments).

In any event, the only issue mentioned in the concurrence that Pierce expressly discusses involves §157(b)(5), which provides that "the district court shall order that personal injury tort and wrongful death claims shall be tried in the district court." Opp'n 41-43. Pierce argues that his proof of claim for defamation and Vickie's counterclaim for tortious interference with a gift were both "personal injury torts" within the meaning of §157(b)(5), and that this Court should not grant certiorari because §157(b)(5) independently compels the conclusion that Vickie's counterclaim was non-core. Opp'n 42-43.

Far from being a reason to deny certiorari, Pierce's argument provides an additional basis for

certiorari review. Courts are in substantial conflict regarding §157(b)(5)'s scope and meaning. *See, e.g.*, *In re Smith*, 389 B.R. 902, 907-08 (Bankr. D. Nev. 2008) (noting at least three conflicting views regarding which "personal injury" claims fall within the statute). Pierce fails to acknowledge that courts have concluded defamation falls outside §157(b)(5)'s scope. *E.g.*, *Massey Energy Co. v. W. Va. Consumers For Justice*, 351 B.R. 348, 351 (E.D. Va. 2006); *In re Davis*, 334 B.R. 874, 878 n.2 (Bankr. W.D. Ky. 2005), *aff'd in part, rev'd in part on other grounds*, 347 B.R. 607 (W.D. Ky. 2006).

Moreover, even courts that have extended §157(b)(5) to defamation have recognized that creditors can impliedly consent to the bankruptcy court entering final judgment on such claims. *Smith*, 389 B.R. at 910-16. *Smith*, for example, concluded that the creditor consented to the bankruptcy court finally adjudicating his defamation claim where he both sought a nondischargeability determination and filed a proof of claim for unliquidated damages and never timely objected to the court adjudicating his defamation claim. *Id.* at 908, 910-16.

As in *Smith*, Pierce filed a proof of claim for defamation and told the bankruptcy court that "[a]ll parties are in agreement that *the amount* of the contingent Proof of Claim filed by [Pierce] shall be *determined by the adversary proceedings filed herein*" and that he would be "happy" and "pleased" to litigate "[his] claim here" because "we did choose this forum." SER 6101-02, 6801 (emphases added). The district

court recognized that Pierce thereby consented to the bankruptcy court adjudicating his defamation claim. App. 266-67 n.17.[6]

In sum, this Court should grant certiorari to resolve the important constitutional and statutory questions posed by the opinion's holding. That such review could (but need not) entail consideration of important §157(b)(5) issues is no reason to deny certiorari.

◆

[6] Moreover, although Pierce attempted to withdraw his claim from the bankruptcy court some two years into the process, the district court rejected that effort, a decision partly "driven by [Pierce's] selection of forum." SER 6185, 6717; *see Sec. Farms v. Int'l Bhd. of Teamsters*, 124 F.3d 999, 1007 n.3 (9th Cir. 1997) (withdrawal motion must be "made as promptly as possible"). Pierce never appealed that ruling.

CONCLUSION

For all the foregoing reasons, the petition for writ of certiorari should be granted.

Dated: August 31, 2010

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JOINT APPENDIX

Supreme Court, U S
FILED
NOV 12 2010
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No. 10-179

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Respondent.

♦

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

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JOINT APPENDIX

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Relevant Docket and Record Entries
UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA
(Southern Division, Santa Ana)
Case No. 8:01-cv-00097-DOC

Original Filing Date[1]	USDC Docket #	USDC Filing Date	Document Title	9th Cir. Excerpts No.
08/14/95	56	04/09/01	Opposition to Application for Letters of Administration	ER 842
04/18/01	67	05/07/01	Injunction to Prevent Relitigation of Judgment and to Prevent Violation of Order of Discharge entered on March 25, 1999	ER 3800

[1] The entries are organized according to the district court docket numbers. However, some of the documents were originally filed in probate or guardianship proceedings in Texas state court or in the underlying adversary proceeding in the bankruptcy court. Accordingly, we have included the original filing date of each document. For the Court's convenience, we have also identified where the documents can be found in the Excerpts of Record ("ER") and Supplemental Excerpts of Record ("SER") filed in the Ninth Circuit.

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01/04/02	383	02/04/02	Transcript of District Court Proceeding	ER 5341
01/08/02	383	02/04/02	Transcript of District Court Proceeding	ER 5363
12/11/01	384	02/04/02	Transcript of District Court Proceeding	ER 4756

12/11/01	384	02/04/02	Transcript of District Court Proceeding	ER 4838
12/12/01	384	02/04/02	Transcript of District Court Proceeding	ER 4892
12/12/01	384	02/04/02	Transcript of District Court Proceeding	ER 4937
12/13/01	384	02/04/02	Transcript of District Court Proceeding	ER 4956
12/14/01	384	02/04/02	Transcript of District Court Proceeding	ER 4973
12/13/01	384	02/04/02	Transcript of District Court Proceeding	ER 5001
12/14/01	384	02/04/02	Transcript of District Court Proceeding	ER 5050
12/17/01	384	02/04/02	Transcript of District Court Proceeding	ER 5095
12/18/01	384	02/04/02	Transcript of District Court Proceeding	ER 5119
12/18/01	384	02/04/02	Transcript of District Court Proceeding	ER 5139

12/19/01	384	02/04/02	Transcript of District Court Proceeding	ER 5154
12/20/01	384	02/04/02	Transcript of District Court Proceeding	ER 5165
12/20/01	384	02/04/02	Transcript of District Court Proceeding	ER 5175
01/02/02	384	02/04/02	Transcript of District Court Proceeding	ER 5309
01/03/02	384	02/04/02	Transcript of District Court Proceeding	ER 5324
01/17/01	388	02/14/02	Motion to Dismiss/Motion to Sever	ER 3442
12/07/01	388	02/14/02	Second Modified Final Judgment	ER 4706
03/07/02	397	03/07/02	U.S. District Court Findings of Fact and Conclusions of Law [*In re Marshall*, 275 B.R. 5 (C.D. Cal. Mar. 7, 2002)]	ER 5390
03/07/02	398	03/07/02	Order Denying Pierce's Motion to Alter or Amend the	ER 5387

			Court's Order Denying Summary Judgment	
03/07/02	400	03/07/02	U.S. District Court Judgment	ER 5385
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05/02/02	419	05/02/02	U.S. District Court's Order Denying Counterclaimant's Motion to Alter or Amend Judgment	ER 126
06/03/02	437	06/03/02	E. Pierce's Marshall's Notice of Appeal	ER 1
—	—	—	Sworn Claim Against Estate (Jan. 21, 1992)	ER 1030
—	—	—	Application for the Appointment of Temporary Guardian (Feb. 8, 1995)	ER 724

—	—	—	Doctor's Form Letter (Feb. 8, 1995	ER 735
—	—	—	J. Howard Marshall, II Order Appointing Temporary Guardian (Feb. 8, 1995)	ER 746
—	—	—	J. Howard Marshall, II Order Confirming Appointment of Temporary Guardian (Feb. 16, 1995)	ER 742
—	—	—	Order Appointing Guardian Ad Litem (May 31, 1995)	ER 788
—	—	—	Agreed Order Appointing Permanent Guardian of the Person (July 28, 1995)	ER 812
—	—	—	Deposition Transcript of E. Pierce Marshall (April 10, 1996)	ER 915

—	—	—	Affidavit of Finley Hilliard (Dec. 31, 1996)	ER 1017
—	—	—	Letter from James E. Myers to Beverly B. Kaufman Regarding the Corporation of Haverford College's Sworn Claim Against Estate (Jan. 17, 1997)	ER 1028
—	—	—	Deposition of Transcript of E. Pierce Marshall, Vol. III (Jan. 31, 1997)	ER 1070
—	—	—	Transcript of Deposition of Harvey Sorensen (April 27, 1998)	ER 1450
—	—	—	Transcript of Defamation Trial (July 4, 1998)	ER 1886
—	—	—	Plaintiff Neiman Marcus' Original Petition (Oct. 24, 1998)	ER 2044

—	—	—	E. Pierce Marshall's Status Report Regarding Debtor's Motion to Strike E. Pierce Marshall's Answer (Nov. 20, 1998)	ER 2058
—	—	—	Plaintiff Vickie Lynn Marshall's Opposition to Defendants' Petition to Enjoin Bankruptcy Proceedings (Oct. 25, 1999)	ER 2512
—	—	—	Transcript of Deposition of Finley Hilliard (Nov. 23, 1999)	ER 2786
—	—	—	Transcript of Deposition of Harvey Sorensen (Dec. 22, 1999)	ER 2794
—	—	—	Transcript of Deposition of Pierce Marshall (Dec. 23, 1999)	ER 2800
—	—	—	Deposition of Pierce Marshall (Dec. 23, 1999)	ER 2168

—	—	—	Transcript of Probate Proceeding (Dec. 27, 1999)	ER 2800
—	—	—	Transcript of Deposition of Edwin Hunter (Dec. 30, 1999)	ER 2822
—	—	—	Transcript of Deposition of Arnold J. Wyche (Jan. 6, 2000)	ER 2877
—	—	—	Transcript of Deposition of Betty Sowell Morgan-Harding (Jan. 21, 2000)	ER 2917
—	—	—	Transcript of Deposition of Betty Sowell Morgan-Harding (Jan. 21, 2000)	ER 2930
—	—	—	Transcript of Deposition of Betty Sowell Morgan-Harding (Jan. 21, 2000)	ER 2951
—	—	—	Transcript of Deposition of Mary Eyvonne Scurlock (Jan. 24, 2000)	ER 2975

—	—	—	Transcript of Deposition of Charlotte W. Fade (Feb. 1, 2000)	ER 2989
—	—	—	Transcript of Deposition of Mary Eyvonne Scurlock (Feb. 4, 2000)	ER 2995
—	—	—	Transcript of Deposition of Jeanette Hunt (Feb. 25, 2000)	ER 3001
—	—	—	Transcript of Deposition of E. Pierce Marshall (Feb. 28, 2000)	ER 3014
—	—	—	Letter to Beverly Kaufman Attaching J. Howard Marshall, III's Supplemental Requests for Disclosure and Designation of Expert Witness (May 31, 2000)	ER 3021
—	—	—	Transcript of Texas Probate Proceeding (Oct. 3, 2000)	ER 3040

—	—	—	Transcript of Texas Probate Proceeding (Oct. 4, 2000)	ER 3042
—	—	—	Transcript of Texas Probate Proceeding (Oct. 5, 2000)	ER 3044
—	—	—	Transcript of Texas Probate Proceeding (Oct. 9, 2000)	ER 3057
—	—	—	Transcript of Texas Probate Proceeding (Oct. 10, 2000)	ER 3060
—	—	—	Transcript of Texas Probate Proceeding (Oct. 11, 2000)	ER 3071
—	—	—	Transcript of Texas Probate Proceeding (Oct. 12, 2000)	ER 3099
—	—	—	Transcript of Texas Probate Proceeding (Oct. 12, 2000)	ER 3101
—	—	—	Transcript of Texas Probate Proceeding (Oct. 16, 2000)	ER 3103

—	—	—	Transcript of Texas Proceeding (Oct. 19, 2000)	ER 3126
—	—	—	Transcript of Texas Proceeding (Oct. 23, 2000)	ER 3131
—	—	—	Transcript of Texas Proceeding (Oct. 24, 2000)	ER 3136
—	—	—	Plaintiff Vickie Lynn Marshall's Fourth Amended Fact Witness List and Supplementation of Prior Interrogatories and Requests for Disclosures (Oct. 13, 2000)	ER 3149
—	—	—	Transcript of Texas Proceeding (Nov. 9, 2000)	ER 3191
—	—	—	Transcript of Texas Proceeding (Nov. 13, 2000)	ER 3195

—	—	—	Transcript of Texas Proceeding (Nov. 29, 2000)	ER 3339
—	—	—	The Marshall Family Defendants' Motion to Exclude Expert Testimony (Nov. 29, 2000)	ER 3322
—	—	—	Transcript of Texas Proceeding (Nov. 30, 2000)	ER 3342
—	—	—	Transcript of Texas Proceeding (Dec. 5, 2000)	ER 3348
—	—	—	Transcript of Texas Proceeding (Dec. 6, 2000)	ER 3350
—	—	—	Transcript of Texas Proceeding (Dec. 18, 2000)	ER 3355
—	—	—	Transcript of Texas Proceeding (Dec. 21, 2000)	ER 3357

—	—	—	Transcript of Texas Proceeding (Jan. 3, 2001)	ER 3373
—	—	—	Transcript of Texas Proceeding (Jan. 5, 2001)	ER 3377
—	—	—	Transcript of Texas Proceeding (Jan. 9, 2001)	ER 3382
—	—	—	Transcript of Texas Proceeding (Jan. 10, 2001)	ER 3385
—	—	—	Transcript of Texas Proceeding (Jan. 12, 2001)	ER 3403
—	—	—	Transcript of Texas Proceeding (Jan. 23, 2001)	ER 3509
—	—	—	Testimony of Vickie Lynn Marshall (Jan. 29, 2001)	ER 3562
—	—	—	Transcript of Texas Proceeding (Feb. 15, 2001)	ER 3636

—	—	—	Transcript of Texas Proceeding (Feb. 20, 2001)	ER 3641
—	—	—	Transcript of Proceeding (May 7, 2001)	ER 3821
—	—	—	Order Reversing and Remanding (Aug. 10, 2001)	ER 3989
—	—	—	Notice of Motion and Motion to Enforce Discharge in Bankruptcy and Vacate the Texas Probate Court Judgment as to Vickie; Memorandum of Points and Authorities; and Declarations of Richard Zook and Howard Stern in Support Thereof (Aug. 31, 2001)	ER 4032
—	—	—	Stipulation of Settled Issues (May 23, 2002)	ER 5469

	—	—	Civil Appeals Docketing Statement (June 3, 2002)	ER 5492
—	—	—	Order Affirming the Bankruptcy Court's First Amended Opinion on Application of Discharge and Order Thereon (Aug. 14, 2002)	ER 5500
—	—	—	Plaintiff's Original Petition	ER 5514
—	—	—	Amended and Consolidated Petition and Will Contest	ER 5523
—	—	—	Petition for Declaratory Judgment and Motion for Trust Disclosure and for Accounting of Income Earned	ER 5614
—	—	—	Docket Sheet	ER 5644
—	—	—	Oral Deposition of J. L. "John Hale, Jr."	ER 5705

Relevant Docket and Record Entries
NINTH CIRCUIT COURT OF APPEALS
Case Nos. # 02-56002, 02-56067.
***Marshall, et al., v. Marshall*, et al.**

Filing Date	9th Circ. Docket #	Document Title
12/30/04	118	FILED OPINION: VACATED and REMANDED (Terminated on the Merits after Oral Hearing: Other; Written, Signed, Published. Robert R. BEEZER, author; Andrew J. KLEINFELD; Richard A. PAEZ.) FILED AND ENTERED JUDGMENT. [02-56002, 02-560671 U.S. Ninth Circuit Court of Appeals Opinion (*In re Marshall*, 392 F.3d 1118 (9th Cir. Dec. 30, 2004)
06/06/06	188	ENTRY UPDATED: This filing only applies to cases 02-56002/ 02-56067. Filed Supreme Court judgment filed and entered in USSC No. 04-1544 on 5/1/06 remanding case to 9th Circuit. (PANEL) [02-56002, 02-56067, 02-56603J- [Edited 03/11/2010 by JI] [Edited 03/11/2010 by JI]. [62308301 [02-56002, 02-56067] (GV)

03/19/10	239	FILED OPINION (ROBERT R. BEEZER, ANDREW J. KLEINFELD and RICHARD A. PAEZ) Neither party shall recover costs on the appellate proceedings subsequent to the Supreme Court's remand. REVERSED AND REMANDED. Judge: RRB Authoring, Judge: AJK concurring. FILED AND ENTERED JUDGMENT. [7271833] [02-56002, 02-56067] (AF)
05/05/10	244	Filed order (ROBERT R. BEEZER, ANDREW J. KLEINFELD and RICHARD A. PAEZ): The petition for panel rehearing and the petition for rehearing en banc DENIED. [7325643J [02-56002, 02-56067] (AF)

SER-10203-10207

United States District Court
Central District of California
(Southern Division – Santa Ana)

5917 Club Oaks Drive
Dallas, Texas 75248-1123
(214)-931-0961
Fax: (713)-931-0961

fax transmittal

to:	Edwin K. Hunter
fax:	(318)-439-2505
from:	E. Pierce Marshall
date:	April 28, 1996
re:	Winston & Bankruptcy matters
pages:	4, including cover sheet.

NOTES: We need to be working on implementing these points while you are away. Call when you have a chance.

CONFIDENTIALITY NOTICE

Unless otherwise indicated or obvious from the nature of this transmittal, the information contained in

or transmitted with this facsimile message is subject to the attorney-client privilege, represents or is a part of attorney work product and/or is confidential and intended solely for the use of the individual or entity named above. If the reader of this message is not the intended recipient (or the employee or agent responsible for delivering it to the intended recipient), you are hereby notified that any dissemination, distribution, reproduction, use of or reliance upon the information contained in this communication by or to anyone other than the designated recipient is strictly prohibited. If you have received this communication in error, please notify the sender by collect telephone immediately. Any facsimilie [sic] erroneously transmitted to you should be immediately returned to the sender by U.S. Mail, or if authorization is granted by the sender, destroyed. I appreciate your cooperation.

ATTORNEY/CLIENT PRIVILEGED
RESPONSE TO HARRY WINSTON JUDGEMENT.

April 28, 1996

1. This is an outrageous judgment: unfair in scope as well as in result. This is the essentially the outcome that Korblit pled in her April 7, 1995, pleading that we agreed directly contradicted the settlement made in open court in March, 1995. Although everyone had the best intentions, the reality is that for the judge to have made a poor decision of such magnitude has to reflect on our strategy and the presentation of the facts. I have no intention of accepting this outcome.

2. ***This is what is required now:***

   A. Determine what action we should take in the VLS Bankruptcy. **We have only a few days to implement our decision.** I need to have claims for my review no later than May 4, 1996.

      1. We must file proofs of claim that provide us the maximum range of options, whether or not we think we can ultimately prevail on each one. A shotgun approach.

      2. Definitely file to rescind the ranch transaction.

      3. Definitely file to rescind the mortgage transaction.

      4. Definitely file a claim to protect the estate and the trust from potential payments to Neiman's and American Express should either of those parties prevail against us.

      5. Definitely file a claim to protect the estate and trust from falling prey to the outrageous position that JHM2's transfers to VLS constituted "gifts" and not "support". We must be prepared for the bankruptcy court to take it.

      6. Definitely file a claim on my libel action as suggested by John Melko.

B. Determine our options for legal recourse on the judgement:

1. Determine how much time we have to move for a new trial, to appeal, or to answer. **I need dates.**

2. Obtain all the pleadings and briefs for review by Judge Hunter. I very much appreciate this very valuable step. It would be most helpful to have the Judge's advice regarding what elements are needed to:

   A. Successfully move for a new trial and prevailing;

   B. Successfully move for an appeal and prevailing.

3. After the Judge has had a chance to review the case, Jeff needs to visit with him to discuss the issues and the Judge's advice. For instance, what happened to our title arguments we were so sure were backed up by solid case law?

* * *

NO. 95-09248

E. PIERCE MARSHALL, Plaintiff, v. VICKIE LYNN HOGAN MARSHALL A.K.A. ANNA NICOLE SMITH, SUZANNE P. KORNBLIT, KORNBLIT AND ASSOCIATES, DIANA E. MARSHALL AND SCHECTER & MARSHALL, L.L.P., Defendants.	§ § § § § § § § § § § §	IN THE DISTRICT COURT DALLAS COUNTY, TEXAS **JURY TRIAL DEMANDED** 191ST JUDICIAL DISTRICT

NOTICE OF NONSUIT OF CLAIMS AGAINST VICKIE LYNN HOGAN MARSHALL A.K.A. ANNA NICOLE SMITH

(Filed May 2, 1996)

Pursuant to Tex. R. Civ. P. 162, E. Pierce Marshall, Plaintiff, hereby gives notice to this Court and to all parties to this suit that he is taking a nonsuit against Vickie Lynn Hogan Marshall a.k.a. Anna Nicole Smith effective immediately on the filing of this notice on this 1st day of May 1996. The Clerk of the Court shall tax court costs against the plaintiff. *This voluntary nonsuit is without prejudice to refiling.* Plaintiff intends to continue prosecuting the claim

against all remaining Defendants other than Vickie Lynn Hogan Marshall a.k.a. Anna Nicole Smith.

Respectfully submitted,

PULS & CHAMBERS, L.L.P.

/s/ Jeffrey W. Chambers
Jeffrey W. Chambers
Bar No. 04075000
W. Kelly Puls
State Bar No. 16393350
Texas Commerce Tower
201 Main Street, Suite 1640
Fort Worth, Texas 76102
Telephone: (817) 338-1717
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Attorneys for Plaintiff
E. Pierce Marshall

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John P. Melko
TBA No. 13919600
VERNER, LIIPFERT, BERNHARD
MCPHERSON AND HAND, CHARTERED
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600 Travis
Houston, Texas 77002
(713) 237-9034
(713) 237-1216 (fax)

Attorneys for Plaintiff,
E. PIERCE MARSHALL

UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA
LOS ANGELES DIVISION

In re	§	Case No.
VICKIE LYNN MARSHALL,	§	LA 96-12510 SB
	§	Chapter 11
Debtor.	§	
	§	
E. Pierce Marshall,	§	Adversary No.
	§	96-01838
Plaintiff,	§	
	§	COMPLAINT TO
v.	§	DETERMINE
	§	DISCHARGE-
Vickie Lynn Marshall,	§	ABILITY OF DEBT
	§	
Defendant.	§	

§ PURSUANT TO 11
§ U.S.C. § 523(a)(6)
§
§ (Filed May 7, 1996)
§
§ Status Conference:
§ 7/10/06
§ Time: 10:00 a.m.
§ Ctrm: 1575

TO THE HONORABLE UNITED STATES BANKRUPTCY JUDGE:

E. Pierce Marshall ("Plaintiff") files this Complaint to Determine Dischargeability of Debt. Pursuant to 11 U.S.C. § 523(a)(6) against Vickie Lynn Marshall, A.K.A. Anna Nicole Smith ("Defendant"), and respectfully states as follows:

I. JURISDICTION

1. The Court has jurisdiction over this adversary proceeding under 28 U.S.C. §§ 1334(b) and 157(a). This adversary proceeding is a core proceeding under 28 U.S.C. §§ 157(b)(2)(J).

2. This adversary proceeding is commenced pursuant to 11 U.S.C. § 523(a)(6) and Rule 7001(1) of the Federal Rules of Bankruptcy Procedure.

II. PARTIES

3. The Plaintiff is an individual and a resident of Dallas, Dallas County, Texas.

4. The Defendant is the individual debtor in the above-captioned Chapter 11 case. The Defendant may be served at 200 Ashdale Avenue, Los Angeles, California 90049 and/or through debtor's counsel, Joel B. Weinberg, Biegenzahn & Weinberg, 21031 Ventura Blvd., Suite 905, Woodland Hills, California 91364.

III. BACKGROUND FACTS

5. On August 4, 1995, J. Howard Marshall, II died. Immediately, his alleged widow, the Defendant, began seeking a settlement from the proceeds of J. Howard Marshall, II's estate. The Defendant and her attorneys, Diana Marshall and Suzanne P. Kornblit ("Kornblit"), instituted a plan to obtain a quick recovery from the estate of J. Howard Marshall, II by embarking on a tortuous smear campaign against E. Pierce Marshall and his family. The Defendant and her lawyers, Kornblit and Diana Marshall sought to humiliate and embarrass E. Pierce Marshall in an effort to get him to influence a settlement in favor of the Defendant and her attorneys from the estate of Plaintiff's deceased father. In their efforts to extort a swift settlement, the Defendant and her attorneys conspired to litigate their case in the press by making slanderous remarks and libelous statements with the intent that they would be published by the press. At the time each of these statements to the press was made, each individual knew that her statement was being recorded or transcribed for publication nationally.

6. After conducting this smear campaign for some time, the defendant and her attorneys briefly ceased their slanderous and libelous remarks to the press and demanded by written communication intended for E. Pierce Marshall that E. Pierce Marshall and representatives of the estate of J. Howard Marshall, II meet and discuss the allegations which the Defendant and her attorneys had made or else the Defendant and her attorneys would resume their campaign against E. Pierce Marshall.

7. Among other statements made to the press by the Defendant's attorneys in furtherance of this civil conspiracy, and in the course and scope of employment by the Defendant, was the statement by Diana Marshall to a reporter from the Houston Chronicle stating that Diana Marshall was "bothered" by "the blizzard of documents that week put in front of Howard Marshall to sign two weeks after his marriage to Anna Nicole Smith. . . . He signed all of them in an almost completely illegible fashion which makes sense because he couldn't read at the time, according to his doctors. . . . J. Howard Marshall's signature appears as sort of a squiggle with only the 'J' clearly readable. . . . The documents signed about two weeks after the oilman's June 27, 1994 marriage, gave the son full control over the J. Howard Marshall, II living trust . . . The effect of it was basically an attempt to remove Howard Marshall from control of his estate."

8. Diana Marshall spoke these defamatory words in the course and scope of her employment for

the Defendant. When Diana Marshall made these statements, she knew that the signatures of J. Howard Marshall, II were legitimate and were witnessed by several other persons. Diana Marshall knew that there was no evidence of any forgery, fraud or over-reaching by E. Pierce Marshall, but chose to make these false statements to the press anyway. She also neglected to tell the press about the other witnesses who were present at the time that J. Howard Marshall, II signed the documents. She also neglected to tell the press that the Defendant is alleging that J. Howard Marshall, II was capable of marrying the Defendant two weeks earlier and of understanding the implications of that act although Diana Marshall suggested in her defamatory comments that J. Howard Marshall, II lacked capacity to sign or did not sign the Trust documents. Despite her actual knowledge that her statements were false and defamatory, Diana Marshall made these statements and thereby committed libel and slander in furtherance of her employment by the Defendant.

9. The defamatory meaning of her statements is clear to any reasonable person. Diana Marshall intended the listener and/or reader of her statements to understand that her statements meant E. Pierce Marshall had used fraud and/or forgery wrongfully to steal control of the J. Howard Marshall, II living trust from his own father. Because the reasonable interpretation of her statements accuses E. Pierce Marshall of one or more criminal acts, Diana Marshall's statements constitute slander and libel *per se*.

The clear defamatory meaning of Diana Marshall's statements is illustrated by a newspaper account published by writer Vincent Lupo. In his account, Lupo stated: "Diana Marshall . . . told the Houston Chronicle recently that the law clearly entitles Smith to half of whatever her late husband earned during their marriage. The lawyer is more worried about the documents Marshall *purportedly* signed two weeks after his marriage to Smith. One of those documents gave the younger Marshall power of attorney over his father whose signature is a mere 'squiggle, with only the J clearly readable. . . .'" It is clear that Diana Marshall's statements taken as a whole were intended to convey either that the signatures were forged ("purportedly signed") or that the documents were signed by a man who was not capable of understanding them.

10. In further attempts to tarnish Plaintiff's reputation and in furtherance of her employment by Smith and the civil conspiracy by the defendants, Kornblit has made numerous defamatory statements to the press about E. Pierce Marshall. In one article, Kornblit characterized E. Pierce Marshall as "greedy and miserly." In another, Kornblit stated that the Defendant "forgives Pierce" and that "our side has always been cooperative . . . but we're just dealing with a real control freak on the other side." These defamatory personal attacks by Kornblit in furtherance of her employment by the Defendant and the civil conspiracy culminated in a letter meant for E. Pierce Marshall's eyes in which Kornblit threatens to

go back to the press if her demands for a meeting with E. Pierce Marshall and other interested parties were not met.

11. At all times relevant to this claim, Diana Marshall and Kornblit were working within the course of scope of their employment for the Defendant. The Defendant was informed of all activities by her attorneys and knew of the smear campaign that her attorneys were conducting in the press. The Defendant participated in the civil conspiracy in an effort to extort a speedy settlement.

12. The conduct described above further constitutes intentional infliction of severe emotional distress by the Defendant and her attorneys. As a proximate result of the Defendant's intentional conduct Plaintiff has suffered serious emotional distress, embarrassment and humiliation.

IV. CAUSE OF ACTION DETERMINATION OF DISCHARGEABILITY UNDER 11 U.S.C. § 523(a)(6)

13. The Plaintiff incorporates each of the above paragraphs by reference.

14. The Defendant is an individual debtor.

15. The Plaintiff's claims against the Defendant are claims arising from the Defendant's willful and malicious acts which resulted in injury to the Plaintiff and/or the Plaintiff's property.

16. Based on the foregoing, any discharge the Defendant may ultimately receive under 11 U.S.C. §§ 1141 or 727 will not discharge E. Pierce Marshall's claims against the Defendant.

WHEREFORE, the Plaintiff respectfully requests that the Court enter a judgment against the Defendant as follows:

1. A determination that the Plaintiff's claims against the Defendant have not been discharged;

2. An order granting the Plaintiff recovery for his reasonable costs and attorney's fees incurred herein and pre- and post-judgment interest as allowed by law; and

3. An order granting the Plaintiff such other relief as is just.

Respectfully submitted this 7 day of May, 1996.

RUBINSTEIN & PERRY

By: /s/ Joanne Mirras Knauss
Joanne Mirras Knauss
355 South Grand Avenue
Thirty-First Floor
Los Angeles, California 30071
(213) 346-1000 – Phone
(213) 680-3275 – Fax

ATTORNEYS FOR E. PIERCE MARSHALL

SER 6020-6027

B10 (Official Form 10) – (Rev. 12/94) 1995 USBC, Central District of California

U.S. Bankruptcy Court, Central District of California

PROOF OF CLAIM

IN RE (Name of Debtor – if individual, enter Last, First, Middle)
VICKIE LYNN MARSHALL

Case Number
LA 96-12510 SB

NOTE: This form should not be used to make a claim for an administrative expense arising after the commencement of the case. A "request" of payment of an administrative expense may be filed pursuant to 11 U.S.C. § 503.

THIS SPACE FOR COURT USE ONLY

Name of Creditor
(The person or entity to whom the debtor owes money or property)
E. PIERCE MARSHALL

Name and address where notices should be sent:
c/o John P. Melko
Verner, Liipfert, Berhard [sic],
McPherson and Hand
600 Travis, Suite 2600
Houston, TX 77002

Telephone No. (713) 225-7200

☐ Check box if you are aware that anyone else has filed a proof of claim relating to your claim. Attach copy of statement giving particulars.

☐ Check box if you have never received any notices from the bankruptcy court in this case.

☐ Check box if the address differs from the address on the envelope sent to you by the court.

ACCOUNT OR OTHER NUMBER BY WHICH CREDITOR IDENTIFIES DEBTOR:

Check here if this claim:
☐ replaces
☐ amends

a previously filed claim, dated: JUN 12 1996
Ans'd _____

1. BASIS FOR CLAIM:

- ☐ Goods sold
- ☐ Services performed
- ☐ Money Loaned
- ☒ Personal injury/wrongful death
- ☐ Taxes
- ☐ Other (Describe briefly): _____
- ☐ Retiree benefits as defined in 11 U.S.C. § 1114(a)
- ☐ Wages, salaries, and compensations (Fill out below)

  Your social security number _____

  Unpaid compensation for services performed

  from _____ (date) to _____ (date)

2. Date Debt was incurred: see attached Ex. "A"

3. If Court Judgment, Date Obtained: N/A

4. CLASSIFICATION OF CLAIM. Under the Bankruptcy Code all claims are classified as one or more of the following: (1) Unsecured nonpriority, (2) Unsecured Priority, (3) Secured. It is possible for part of a claim to be in one category and part in another. CHECK THE APPROPRIATE BOX OR BOXES that best describe your claim and STATE THE AMOUNT OF THE CLAIM AT TIME CASE FILED.

☐ SECURED CLAIM $_____

Attach evidence of perfection of security interest

Brief Description of Collateral:

- ☐ Real Estate
- ☐ Motor Vehicle
- ☐ Other:_____

Amount of arrearage and other charges included in secured claim above, if any $_____

☒ UNSECURED NONPRIORITY CLAIM $ Unliquidated

A claim is unsecured if there is no collateral or lien on property of the debtor securing the claim or to the extent that the value of such property is less that the amount of the claim.

*see attached Exhibit "A"

☐ UNSECURED PRIORITY CLAIM $_____

Specify the priority of the claim.

- ☐ Wages, salaries, or commissions (up to $4000),* earned not more than 90 days before filing of the bankruptcy petition or cessation of the debtor's business, whichever is earlier) – 11 U.S.C. § 507(a)(3)
- ☐ Contributions to an employee benefit plan – 11 U.S.C. § 507(a)(4)
- ☐ Up to $1,800* of deposits toward purchase, lease, or rental of property or services for personal, family, or household use – 11 U.S.C. § 507(a)(6)
- ☐ Taxes or penalties of governmental units – 11 U.S.C. § 507(a)(8)
- ☐ Other – 11 U.S.C. § 507(a) _____

*Amounts are subject to adjustment on 4/1/96 and every 3 years thereafter with respect to cases commenced on or after the date of adjustment.

5. TOTAL AMOUNT OF CLAIM AT TIME CASE FILED:

$ Unliquidated (Unsecured)	$ _____ (Secured)	$ _____ (Priority)	$ Unliquidated (Total)

☐ Check this box if claim includes charges in addition to the principal amount of the claim. Attach itemized statement of all additional charges.

6. CREDITS AND SETOFFS. The amount of all payments on this claim has been credited and deducted for the purpose of making this proof of claim. In filing this claim, claimant has deducted all amounts that claimant owes to debtor.

THIS SPACE FOR COURT USE ONLY

7. SUPPORTING DOCUMENTS: *Attach copies of supporting documents*, such as promissory notes, purchase orders, invoices, itemized statements of running accounts, contracts, court judgments, or evidence of security interests. If the documents are not available, explain. If the documents are voluminous, attach a summary.

8. TIME-STAMPED COPY: To receive an acknowledgment of the filing of your claim, enclose a stamped, self-addressed envelope and copy of this proof of claim.

Date

6/11/96

Sign and print the name and title, if any, of the creditor or other person authorized to file this claim (attach copy of power of attorney, if any)

/s/ Joanne Mirras Knauss
Joanne Mirras Knauss, Attorney
for E. Pierce Marshall

Penalty for presenting fraudulent claim: Fine of up to $500,000 or imprisonment for up to 5 years, or both. 18 U.S.C. §§ 152 and 3571.

EXHIBIT A

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Attorneys for Plaintiff,
E. PIERCE MARSHALL

UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA
LOS ANGELES DIVISION

In re	§	Case No.
VICKIE LYNN MARSHALL,	§	LA 96-12510 SB
Debtor.	§	Chapter 11
E. Pierce Marshall,	§	Adversary No.
Plaintiff,	§	96-01838
v.	§	COMPLAINT TO DETERMINE DISCHARGE-ABILITY OF DEBT
Vickie Lynn Marshall,	§	
Defendant.	§	

§ PURSUANT TO 11
§ U.S.C. § 523(a)(6)
§
§ (Filed May 7, 1996)
§
§ Status Conference:
§ 7/10/06
§ Time: 10:00 a.m.
§ Ctrm: 1575

TO THE HONORABLE UNITED STATES BANKRUPTCY JUDGE:

E. Pierce Marshall ("Plaintiff") files this Complaint to Determine Dischargeability of Debt Pursuant to 11 U.S.C. § 523(a)(6) against Vickie Lynn Marshall, A.K.A. Anna Nicole Smith "Defendant" and respectfully states as follows:

I. JURISDICTION

1. The Court has jurisdiction over this adversary proceeding under 28 U.S.C. §§ 1334(b) and 157(a). This adversary proceeding is a core proceeding under 28 U.S.C. §§ 157(b)(2)(J).

2. This adversary proceeding is commenced pursuant to 11 U.S.C. § 523(a)(6) and Rule 7001(1) of the Federal Rules of Bankruptcy Procedure.

II. PARTIES

3. The Plaintiff is an individual and a resident of Dallas, Dallas County, Texas.

4. The Defendant is the individual debtor in the above-captioned Chapter 11 case. The Defendant may be served at 20 Ashdale Avenue, Los Angeles, California 90049 and/or through debtor's counsel. Joel B. Weinberg, Biegenzahn & Weinberg, 21031 Ventura Blvd., Suite 905, Woodland Hills, California 91364.

III. BACKGROUND FACTS

5. On August 4, 1995, J. Howard Marshall, II died. Immediately, his alleged widow, the Defendant, began seeking a settlement from the proceeds of J. Howard Marshall, II's estate. The Defendant and her attorneys, Diana Marshall and Suzanne P. Kornblit ("Kornblit"), instituted a plan to obtain a quick recovery from the estate of J. Howard Marshall, II by embarking on a tortuous smear campaign against E. Pierce Marshall and his family. The Defendant and her lawyers, Kornblit and Diana Marshall sought to humiliate and embarrass E. Pierce Marshall in an effort to get him to influence a settlement in favor of the Defendant and her attorneys from the estate of Plaintiff's deceased father. In their efforts to extort a swift settlement, the Defendant and her attorneys conspired to litigate their case in the press by making slanderous remarks and libelous statements with the intent that they would be published by the press. At the time each of these statements to the press was made, each individual knew that her statement was being recorded or transcribed for publication nationally.

6. After conducting this smear campaign for some time, the defendant and her attorneys briefly ceased their slanderous and libelous remarks to the press and demanded by written communication intended for E. Pierce Marshall that E. Pierce Marshall and representatives of the estate of J. Howard Marshall, II meet and discuss the allegations which the Defendant and her attorneys had made or else the Defendant and her attorneys would resume their campaign against E. Pierce Marshall.

7. Among other statements made to the press by the Defendant's attorneys in furtherance of this civil conspiracy, and in the course and scope of employment by the Defendant, was the statement by Diana Marshall to a reporter from the Houston Chronicle stating that Diana Marshall was "bothered" by "the blizzard of documents that week put in front of Howard Marshall to sign two weeks after his marriage to Anna Nicole Smith. . . . He signed all of them in an almost completely illegible fashion which makes sense because he couldn't read at the time, according to his doctors. . . . J. Howard Marshall's signature appears as sort of a squiggle with only the 'J' clearly readable. . . . The documents signed about two weeks after the oilman's June 27, 1994 marriage, gave the son full control over the J. Howard Marshall, II living trust . . . The effect of it was basically an attempt to remove Howard Marshall from control of his estate."

8. Diana Marshall spoke these defamatory words in the course and scope of her employment for

the Defendant. When Diana Marshall made these statements, she knew that the signatures of J. Howard Marshall, II were legitimate and were witnessed by several other persons. Diana Marshall knew that there was no evidence of any forgery, fraud or over-reaching by E. Pierce Marshall, but chose to make these false statements to the press anyway. She also neglected to tell the press about the other witnesses who were present at the time that J. Howard Marshall, II signed the documents. She also neglected to tell the press that the Defendant is alleging that J. Howard Marshall, II was capable of marrying the Defendant two weeks earlier and of understanding the implications of that act although Diana Marshall suggested in her defamatory comments that J. Howard Marshall, II lacked capacity to sign or did not sign the Trust documents. Despite her actual knowledge that her statements were false and defamatory, Diana Marshall made these statements and thereby committed libel and slander in furtherance of her employment by the Defendant.

9. The defamatory meaning of her statements is clear to any reasonable person. Diana Marshall intended the listener and/or reader of her statements to understand that her statements meant E. Pierce Marshall had used fraud and/or forgery wrongfully to steal control of the J. Howard Marshall, II living trust from his own father. Because the reasonable interpretation of her statements accuses E. Pierce Marshall of one or more criminal acts, Diana Marshall's statements constitute slander and libel *per se*.

The clear defamatory meaning of Diana Marshall's statements is illustrated by a newspaper account published by writer Vincent Lupo. In his account, Lupo stated: "Diana Marshall . . . told the Houston Chronicle recently that the law clearly entitles Smith to half of whatever her late husband earned during their marriage. The lawyer is more worried about the documents Marshall *purportedly* signed two weeks after his marriage to Smith. One of those documents gave the younger Marshall power of attorney over his father whose signature is a mere 'squiggle, with only the J clearly readable. . . .'" It is clear that Diana Marshall's statements taken as a whole were intended to convey either that the signatures were forged ("purportedly signed") or that the documents were signed by a man who was not capable of understanding them.

10. In further attempts to tarnish Plaintiff's reputation and in furtherance of her employment by Smith and the civil conspiracy by the defendants, Kornblit has made numerous defamatory statements to the press about E. Pierce Marshall. In one article, Kornblit characterized E. Pierce Marshall as "greedy and miserly." In another, Kornblit stated that the Defendant "forgives Pierce" and that "our side has always been cooperative . . . but we're just dealing with a real control freak on the other side." These defamatory personal attacks by Kornblit in furtherance of her employment by the Defendant and the civil conspiracy culminated in a letter meant for E. Pierce Marshall's eyes in which Kornblit threatens to

go back to the press if her demands for a meeting with E. Pierce Marshall and other interested parties were not met.

11. At all times relevant to this claim, Diana Marshall and Kornblit were working within the course of scope of their employment for the Defendant. The Defendant was informed of all activities by her attorneys and knew of the smear campaign that her attorneys were conducting in the press. The Defendant participated in the civil conspiracy in an effort to extort a speedy settlement.

12. The conduct described above further constitutes intentional infliction of severe emotional distress by the Defendant and her attorneys. As a proximate result of the Defendant's intentional conduct Plaintiff has suffered serious emotional distress, embarrassment and humiliation.

IV. CAUSE OF ACTION DETERMINATION OF DISCHARGEABILITY UNDER 11 U.S.C. § 523(a)(6)

13. The Plaintiff incorporates each of the above paragraphs by reference.

14. The Defendant is an individual debtor.

15. The Plaintiff's claims against the Defendant are claims arising from the Defendant's willful and malicious acts which resulted in injury to the Plaintiff and/or the Plaintiff's property.

16. Based on the foregoing, any discharge the Defendant may ultimately receive under 11 U.S.C. §§ 1141 or 727 will not discharge E. Pierce Marshall's claims against the Defendant.

WHEREFORE, the Plaintiff respectfully requests that the Court enter a judgment against the Defendant as follows:

1. A determination that the Plaintiff's claims against the Defendant have not been discharged;

2. An order granting the Plaintiff recovery for his reasonable costs and attorney's fees incurred herein and pre- and post-judgment interest as allowed by law; and

3. An order granting the Plaintiff such other relief as is just.

Respectfully submitted this 7 day of May, 1996.

RUBINSTEIN & PERRY

By: /s/ Joanne Mirras Knauss
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ATTORNEYS FOR PLAINTIFF
E. PIERCE MARSHALL

UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA

In re	§	Case No. LA 96-12510 SB
VICKIE LYNN MARSHALL,	§	Chapter 11
Debtor.	§	Adversary No. 96-01838
E. Pierce Marshall,	§	ANSWER AND AFFIRMATIVE DEFENSES OF E. PIERCE MARSHALL TO COUNTERCLAIM BY VICKIE LYNN MARSHALL AGAINST E. PIERCE MARSHALL.
Plaintiff,	§	
v.	§	
Vicki Lynn Marshall,	§	
Defendant.	§	

Vickie Lynn Marshall, Counterclaimant, v. E. Pierce Marshall, Counterdefendant.	§ § § § § § § § § §	(Filed Jul. 8, 1996) STATUS CONFERENCE: July 10, 1996 TIME: 10:00 a.m. CTRM:1575 Roybal Federal Building 255 East Temple Street Los Angeles, CA 90012

TO THE HONORABLE UNITED STATES BANKRUPTCY JUDGE:

COMES NOW E. Pierce Marshall and files this Answer in response to the Counterclaim filed filed [sic] by Vickie Lynn Marshall, A.K.A. Anna Nicole Smith ("Defendant"), Against E. Pierce Marshall, and alleges, admits, and denies as follows:

ANSWER TO COUNTERCLAIMS

1. Plaintiff denies that this Court has jurisdiction over any of Defendant's counterclaims, except for those counterclaims which relate to alleged avoidance actions. With respect to the alleged avoidance actions, because the subject matter of virtually all of the alleged avoidance actions is the subject of pending actions or court orders in a probate action in state court in Louisiana, this Court should abstain from exercising jurisdiction over the alleged avoidance actions. Plaintiff denies the allegations in the third sentence of paragraph 1 because none of the counterclaims arise in the Debtor's Chapter 11 case.

To the extent that jurisdiction may be concurrent, this Court must abstain pursuant to 28 U.S.C. § 1334. Plaintiff reserves his right to move timely for abstention.

2. Denied.

3. Admitted, except to the extent that a Trustee is appointed in this case.

4. Admitted.

5. Plaintiff denies the allegations contained in paragraph 5 to the extent that the Defendant alleges that Plaintiff is a "self-professed creditor," and admits the remaining allegations in paragraph 5.

6. Denied.

7. Denied.

8. Plaintiff admits that J. Howard Marshall and the Defendant did not execute a prenuptial agreement. However, the Defendant and her counsel had agreed upon such an agreement, which the parties had negotiated over many months. The agreement had not yet been finalized at the time when the Defendant "eloped" with J. Howard Marshall, who – then in his late eighties – was physically weak and wheelchair bound. Plaintiff denies the remaining allegations in paragraph 8.

9. Denied. In fact, as is the subject of probate court litigation in Houston, Texas, the so-called "Elder Son" has not been a beneficiary under Mr. Marshall's will since the early 1980's. Upon information and

belief, counsel for Defendant and for "Elder Son" are sharing information in the pending litigation in Louisiana and Texas.

10. Denied.

11. Denied. In fact, in approximately 1982, at least 10 years prior to ever having met the Defendant, J. Howard Marshall had established the J. Howard Marshall, II Living Trust as part of his estate planning. This trust is presently the subject of litigation in state court in Louisiana. The "Elder Son" and other purported creditors are parties to that action.

12. Denied. During his brief marriage to the Defendant, Mr. Marshall transferred millions of dollars of property, including substantial amounts of cash (including currency), to the Defendant. Plaintiff has been unable to locate many of these assets in the Defendant's Schedule of Assets.

13. Plaintiff admits that there is an action pending in Louisiana state court. Plaintiff further admits that there is an action pending in Texas state court. Plaintiff denies that either state court action is directly or indirectly against the Defendant. Many of the allegations in this paragraph 13 regarding the Defendant's alleged entitlement have been resolved either by orders or agreement in the litigation in a Texas state court proceeding initiated by the Defendant, which is still pending, but not referenced in the Counterclaim. The statements of the Defendant (and her counsel) in this paragraph 13 regarding the other courts are scandalous. Plaintiff, as subject to the

jurisdiction of those courts, will report the statements to those courts.

14. Denied.

ANSWER TO FIRST COUNTERCLAIM

15. The allegations stated in paragraph 15 do not require a response. Plaintiff reasserts and incorporates its responses to paragraphs 1-14.

16. Denied.

17. To the extent the statements in paragraph 17 constitute a legal conclusion or legal argument, no response is necessary. However, to the extent that the Defendant intends the statement in paragraph 17 to be factual allegations, such allegations are denied. Under the Living Trust, Mr. Marshall received all income from the trust. The Defendant spent all of the income Mr. Marshall received. Mr. Marshall then borrowed money for the Defendant, which she also spent, leaving him in debt. Defendant earned substantial sums on her own in which Mr. Marshall had a community interest. Defendant kept these funds from the community estate. Defendant spent vast sums of money in fraud of the community estate, including on a series of other individuals before and after the marriage.

18. Denied.

19. Denied.

20. Denied. The Defendant's profligate spending, coupled with her failure to manage appropriately (or even keep track of) millions of dollars of assets transferred to her, was the cause of her insolvency.

21. Denied. Again, it was the Defendant's actions alone which led to her insolvency.

22. Denied.

23. Denied.

24. To the extent the statements in paragraph 24 constitute a legal conclusion or legal argument, no response is necessary. However, to the extent that the Defendant intends that the statement in paragraph 24 to be factual allegations, such allegations are denied.

25. Denied.

ANSWER TO SECOND COUNTERCLAIM

26. The allegations stated in paragraph 26 do not require a response. Plaintiff reasserts and incorporates its responses to paragraphs 1-25.

27. The allegations stated in paragraph 27 regarding the relief the Defendant seeks do not require a response. Plaintiff denies the remainder of paragraph 27. Plaintiff admits that the Defendant is seeking an injunction for the purposes stated, and notes that the Defendant is really seeking to have this court enjoin the Louisiana and Texas courts, which have appropriate jurisdiction over purely state

law matters, namely trust, probate and family law matters. These are matters which federal courts abstain from hearing, 28 U.S.C. 1334, and are matters which, if removed, would properly be remanded to the state courts.

28. To the extent the statements in paragraph 28 constitute a legal conclusion or legal argument, no response is necessary. However, to the extent that the Defendant intends the statement in paragraph 28 to be factual allegations, such allegations are denied.

29. Denied. The Texas and Louisiana actions were commenced pre-petition, and the Defendant has not filed any claim in either action, nor has she been an heir under Mr. Marshall's will. The Defendant clearly has had actual notice of the two proceedings, and has chosen not to participate in either. Moreover, Debtor has abandoned her own lawsuit in Texas where some of these matters were raised, and where she was represented by counsel. Debtor's own Schedule of Assets state an absolute admission of the jurisdiction of those courts and state her intention to join in those proceedings.

30. To the extent the statements in paragraph 30 constitute a legal conclusion or legal argument, no response is necessary. However, to the extent that the Defendant intends the statement in paragraph 30 to be factual allegations, such allegations are denied.

ANSWER TO THIRD COUNTERCLAIM

31. The allegations stated in paragraph 31 do not require a response. Plaintiff reasserts and incorporates its responses to paragraphs 1-30.

32. Denied. These allegations are in at least partial contravention of a prior state court order to which the Debtor was a party, as set forth above.

33. Denied.

34. Denied.

ANSWER TO FOURTH COUNTERCLAIM

35. The allegations stated in paragraph 35 do not require a response. Plaintiff reasserts and incorporates its responses to paragraphs 1-34.

36. Plaintiff has insufficient knowledge to admit or deny the allegations contained in paragraph 36, and therefore denies such allegations.

37. Denied. As stated above, these allegations are at least in part directly controverted by one or more state court orders to which the Defendant is a party. Defendant spent virtually no time with Mr. Marshall during the marriage and was frequently unreachable for long periods of time. These unexplained absences caused Mr. Marshall extreme emotional distress. Defendant would always solicit and often obtained large gifts or transfers from Mr. Marshall while he was recovering from these bouts of distress.

38. Denied.

39. Denied.

ANSWER TO FIFTH COUNTERCLAIM

40. The allegations stated in paragraph 40 do not require a response. Plaintiff reasserts and incorporates its responses to paragraphs 1-39.

41. Denied. Upon information and belief, the Defendant incurred obligations in excess of Mr. Marshall's income from the Living Trust, while she kept all money she earned during the relevant time period.

42. Denied.

43. Denied.

44. Denied.

45. Denied.

ANSWER TO SIXTH COUNTERCLAIM

46. The allegations stated in paragraph 46 do not require a response. Plaintiff reasserts and incorporates its responses to paragraphs 1-45.

47. Denied. The Defendant has no factual basis to support her allegations in this paragraph 47, and is affirmatively attempting to mislead this Court through those allegations. The Plaintiff also notes that although the Defendant is the subject of a prepetition

libel and slander action brought by the Plaintiff in Texas (and, in fact, one of her counsel in this action, Diana E. Marshall, is a co-defendant in that action), the Defendant failed to list this liability in her Schedules.

48. Denied.

49. Denied.

ANSWER TO SEVENTH COUNTERCLAIM

50. The allegations stated in paragraph 50 do not require a response. Plaintiff reasserts and incorporates its responses to paragraphs 1-49.

51. Mr. Marshall transferred millions of dollars in cash (i.e. currency), cash equivalents, and other property to the Defendant to fulfill any alleged obligation he may have had. Plaintiff denies the remainder of this paragraph 51.

52. Denied.

53. Denied.

54. Denied.

55. Denied.

ANSWER TO EIGHTH COUNTERCLAIM

56. The allegations stated in paragraph 56 do not require a response. Plaintiff reasserts and incorporates its responses to paragraphs 1-55.

57. Denied.

58. Denied.

59. Denied.

60. Denied.

ANSWERS TO NINTH COUNTERCLAIM

61. The allegations stated in paragraph 61 do not require a response. Plaintiff reasserts and incorporates its responses to paragraphs 1-60.

62. To the extent the statements in paragraph 62 constitute a legal conclusion or legal argument, no response is necessary. However, to the extent that the Defendant intends the statement in paragraph 62 to be factual allegations, such allegations are denied. Plaintiff denies the remainder of paragraph 62.

63. Denied.

64. Denied.

65. Denied.

ANSWER TO TENTH COUNTERCLAIM

66. The allegations stated in paragraph 66 do not require a response. Plaintiff reasserts and incorporates its responses to paragraphs 1-65.

67. The allegations stated in paragraph 67 regarding the relief the Defendant seeks do not require

a response. Plaintiff denies the remainder of paragraph 67.

ANSWER TO ELEVENTH COUNTERCLAIM

68. The allegations stated in paragraph 68 do not require a response. Plaintiff reasserts and incorporates its responses to paragraphs 1-67.

69. The allegations stated in paragraph 69 regarding the relief the Defendant seeks do not require a response. Plaintiff denies the remainder of paragraph 69. Plaintiff notes that the Louisiana court, with appropriate jurisdiction over the J. Howard Marshall's probate estate, has already approved an accounting of Mr. Marshall's assets as of his death. These rulings are *res judicata*.

ANSWER TO TWELFTH COUNTERCLAIM

70. The allegations stated in paragraph 70 do not require a response. Plaintiff reasserts and incorporates its responses to paragraphs 1-69.

71. The allegations stated in paragraph 71 are so vague as to be unanswerable, and are therefore denied.

72. Plaintiff denies that the Defendant is entitled to recover against the Plaintiff under any of the Defendant's stated causes of action, and notes that the Defendant's true objective in her Counterclaim is to have this federal bankruptcy court litigate trust

and estate matters which are already in litigation in state courts in Texas and Louisiana.

RESERVATION OF RIGHTS

73. Plaintiff believes that the factual allegations and legal arguments are not based on a reasonable inquiry with respect to either factual or legal matters and reserves his right to seek appropriate sanctions.

AFFIRMATIVE DEFENSES

FIRST AFFIRMATIVE DEFENSE

6. The Defendant has failed to state facts sufficient to state a basis for a claim for relief.

SECOND AFFIRMATIVE DEFENSE

7. Answering further, Defendant's Counterclaim: (1) has failed to show with any specificity what, if any, assets were transferred, and (2) has failed to show the Defendant had any interest in the assets allegedly transferred.

THIRD AFFIRMATIVE DEFENSE

8. Answering further, because the Defendant has failed to show that she had any legal interest in any assets which Plaintiff allegedly transferred, any resulting insolvency cannot be the result of such alleged transfers.

FOURTH AFFIRMATIVE DEFENSE

9. Answering further, many of the matters raised in the Counterclaim have been directly disposed of by agreed order to which the Defendant was a party in the Texas state court litigation, and that order is res judicata in the present action as to such allegations. Defendant is further collaterally estopped.

FIFTH AFFIRMATIVE DEFENSE

10. Answering further, with respect to Defendant's Fifth Counterclaim, the Defendant has failed to allege any facts which show that Plaintiff had any duty to the Defendant.

SIXTH AFFIRMATIVE DEFENSE

11. Answering further, Defendant lacks standing to assert a claim for relief as set forth in the Counterclaims.

SEVENTH AFFIRMATIVE DEFENSE

12. Answering further, with respect to the Defendant's abuse of process claim, Plaintiff has a libel and slander action pending in Texas state court, which was filed pre-petition. Plaintiff has filed a proof of claim in this case to protect his interests when a judgment is obtained in that lawsuit against the Defendant. The Defendant lists Plaintiff as a creditor in her Financial Statement, though fails to identify

the nature and amount of Plaintiff's claim. Also, Plaintiff in his role as executor of the Succession of J. Howard Marshall has moved in the present proceeding for the appointment of a Trustee to look into serious allegations regarding the Defendant. That motion was joined by a judgment creditor and granted in part by this Court. An Examiner has been appointed. One of the Examiner's duties is to determine whether appointment of a Trustee would be appropriate.

WHEREFORE, PREMISES CONSIDERED, Plaintiff requests that the Court enter a judgment denying the relief requested in the Defendant's Complaint in all respects, granting Plaintiff its [sic] attorneys' fees, costs and expenses incurred in the defense of this action, and granting Plaintiff such other and further relief to which he is entitled.

DATED: July 8, 1996 Respectfully submitted,

VERNER, LIPFERT,
BERNHARD, MCPHERSON
AND HAND
John P. Melko

and

RUBINSTEIN & PERRY,
A Professional Corporation

By: /s/ Joanne Mirras Knauss
JOANNE MIRRAS KNAUSS
Attorneys for E. Pierce Marshall

[Verification And Proof Of Service Omitted In Printing]

ER-2019-2033

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ATTORNEYS FOR PLAINTIFF/
COUNTERDEFENDANT
E. PIERCE MARSHALL

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA
WESTERN DIVISION

In re	§	Case No.: CV 98-7686 WDK
VICKIE LYNN MARSHALL,	§	Bk. Case No. LA 96-12510 SB
Debtor.	§	Chapter 11
E. Pierce Marshall,	§	Adversary No. 96-01838
Plaintiff,	§	**NOTICE OF MOTION AND MOTION OF E. PIERCE MARSHALL FOR WITHDRAWAL OF REFERENCE OF ADVERSARY PROCEEDINGS;**
v.	§	
Vickie Lynn Marshall,	§	
Defendant.	§	

Vickie Lynn Marshall, Counterclaimant v. E. Pierce Marshall, Counterdefendant.	§	**MEMORANDUM OF POINTS AND AUTHORITIES** (Filed Sep. 22, 1998) [28 U.S.C. § 157(d); Fed.R. Bankr. P. 5011; Local Bankruptcy Rule 111(10)] Date: October 19, 1998 Time: 3:00 pm. Place: 312 North Spring Street Los Angeles, CA 90012

TO THE HONORABLE JUDGE OF THE UNITED STATES BANKRUPTCY COURT, ALL INTERESTED PARTIES AND THEIR ATTORNEYS OF RECORD:

NOTICE OF MOTION

PLEASE TAKE NOTICE that plaintiff/counter-defendant E. Pierce Marshall ("Movant") hereby moves the District Court for an order withdrawing the reference of the above-captioned adversary proceeding. The motion will be heard on October 19, 1998 at 3:00 p.m., or as soon thereafter as may be heard in the courtroom designated by the Clerk of the United States District Court within the United States Courthouse, located at 312 N. Spring Street, Los Angeles, California.

MOTION

Pursuant to 28 U.S.C. § 157(d), the Movant requests that this Court withdraw the reference of this adversary proceeding, so that the case will proceed before the District Court for purposes of the mandatory status conference, dispositive motions and trial. The Motion is based upon the accompanying Memorandum of Points and Authorities, all pleadings and files in the above-referenced adversary proceeding and main bankruptcy case, and upon such further oral and written evidence and argument as the Court may consider at any hearing. The grounds constituting "cause" for withdrawal under 28 U.S.C. § 157(d) are set forth below in the Movant's Memorandum of Points and Authorities.

This Motion is made following the conference of counsel pursuant to Local Rule 7.4.1, which took place on August 28, 1998.

Dated: September 22 1998.

VERNER, LIIPFERT, BERNHARD,
MCPHERSON & HAND CHTD.

By: /s/ [Illegible] for
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ATTORNEYS FOR E. PIERCE MARSHALL

* * *

MEMORANDUM OF POINTS AND AUTHORITIES

I. INTRODUCTION

This Court has recently withdrawn the reference of another adversary proceeding which is related to the above-captioned bankruptcy case, styled *Vickie Lynn Marshall v. Finley Hilliard, individual, as trustee of the J. Howard Marshall Living Trust and as executor of the Succession of J. Howard Marshall II (Louisiana); Kenneth Farrar, an individual, as trustee of the J. Howard Marshall Living Trust; and Marshall Petroleum, Inc., a Texas Corporation*, Adv. No. 98-01159 (the "MPI Adversary Proceeding"). The

MPI Adversary Proceeding and this case involve *identical* allegations and causes of action by the Debtor. Based on the grounds set out below, the Movant requests that this Court withdraw its reference of *this* adversary proceeding from the Bankruptcy Court so that this controversy may proceed before this Court for dispositive motions and trial. Also as discussed below, Movant's underlying Complaint requires an adjudication of personal injury tort claims thereby mandating withdrawal of the reference for that part of the adversary proceeding. With regard to the balance of the case, judicial economy and the risk of inconsistent judgments in this case militate heavily in favor of withdrawal of the reference in this case. If this Court withdraws the reference, the Movant will seek consolidation of the two cases pursuant to Fed. R. Civ. P. 42.

II. BACKGROUND

A. Procedural History of the Adversary Proceeding.

The Debtor filed her voluntary petition for relief under Chapter 11 on January 25, 1996. This adversary proceeding commenced when Mr. E. Pierce Marshall filed his Complaint to Determine Dischargeability of Debt Pursuant to 11 U.S.C. § 523 (a)(6) (the "Complaint") on May 7, 1996. The Complaint sought a determination that the Debtor's pre-petition statements to the press regarding Mr. Marshall were defamatory, and were made willfully and maliciously,

and thus his damages arising therefrom should be excepted from discharge.

The Complaint was necessary because Mr. Marshall's pre-petition state court litigation against the Debtor and two of her counsel had been stayed by the bankruptcy filing. The Debtor was severed from the pre-petition litigation which proceeded to a settlement with one of the remaining defendants, and to a jury verdict in favor of Mr. Marshall against the other remaining defendant.[1] There has not yet been a judicial determination that the *Debtor's* statements were defamatory. Procedurally and jurisdictionally this is important as discussed below. Factually, it is important because the defense asserted by the defendant who went to trial (one of the lawyers listed as Debtor's co-counsel in this adversary proceeding) is virtually identical to the Debtor's claims herein.

The Debtor filed her Answer and Counterclaim Against Plaintiff under 11 U.S.C. §§ 544, 550 and Applicable State Law (the "Counterclaim," attached as Exhibit "B") on June 14, 1996. In her Counterclaim, the Debtor asserts the following causes of action against the Movant:

(1) Fraudulent transfers under 11 U.S.C. §§ 544, 550 and applicable state law.

[1] A true an [sic] correct copy of the state court's charge to the jury and the jury's verdict is attached hereto as Exhibit "A".

(2) Injunctive relief regarding alleged transfers from J. Howard Marshall, II ("JHM II"), the Debtor's deceased husband.

(3) Conversion.

(4) Tortious interference with inheritance.

(5) Breach of fiduciary duty.

(6) Abuse of judicial process.

(7) Fraud.

(8) Breach of an unidentified contract.

(9) The Debtor seeks a determination that she is a third party beneficiary of an unidentified contract.

(10) Imposition of a constructive trust.

(11) The Debtor seeks an accounting.

(12) The Debtor seeks contribution or indemnity for the claims against her in the bankruptcy case.

Even a cursory review of the Counterclaim demonstrates it is nothing more than a state law probate/family law dispute disguised in bankruptcy avoidance action clothing. Mr. Marshall filed a Motion to Dismiss, which was denied, and an Answer. Thereafter, he filed a Motion to Abstain, on January 6, 1997, which was also denied.

Since that time, the parties have been completely unable to move forward to the merits of this case. Instead, the Debtor has conducted an ongoing discovery

war. The Debtor's efforts mirror the tactics used by another will contestant, Mr. Marshall's brother, J. Howard Marshall III ("JHM III") in Texas Probate Court. Not only has the Debtor closely monitored the Texas probate proceeding of JHM III, but she filed her own petition in the Probate Court nearly identical to what she has filed here. A true and correct copy is attached as Exhibit "C." She has also moved to be included in the protective order entered in the JHM III litigation. A true and correct copy of her motion is attached as Exhibit "D." Moreover, the Debtor still has pending in Probate Court other pre-petition actions where she is the plaintiff or movant.

After nearly 30 months since the date of the Complaint, neither the deposition of Mr. Marshall nor the Debtor has been completed. Additionally, depositions of only three other potential witnesses out of a total of approximately twenty have been started. Not a single one of these depositions (all of which were started by the Debtor) has been completed. The Debtor's entire effort, again modeled on the Texas Probate case, has been to seek "death penalty" sanctions against Mr. Marshall for the alleged failure to produce, or cause third-parties to produce, documents. To date, there have been at least five discovery hearings held in this case.

B. The MPI Adversary Proceeding.

On January 23, 1998, the Debtor initiated the MPI Adversary Proceeding against Marshall Petroleum,

Inc., Finley Hilliard and Kenneth Farrar (as individuals and in their representative capacities) by filing a Complaint for Turnover of Property of the Estate, for Injunctive Relief, and for Damages (the "MPI Complaint"). A copy of the MPI Complaint is attached as Exhibit "E".[2] In the MPI Complaint, the Debtor asserts *the same causes of action* against the defendants as those the Debtor asserts against the Movant in the Marshall Adversary Proceeding.

On July 24, 1998, this Court entered an Order withdrawing the reference of the MPI Adversary Proceeding for dispositive motions and trial, and further providing that discovery and other pretrial matters would take place before the Bankruptcy Court (the "MPI Withdrawal Order").

C. The Debtor's Related Litigation.

Beyond the overlapping claims the Debtor asserts against a number of parties in the Marshall Adversary Proceeding and the MPI Adversary Proceeding, the Debtor is litigating virtually *identical* claims against all the above-referenced defendants in probate court in Houston, Texas. *See* Exhibit "C" – a copy of the Debtor's Amended and Consolidated Petition and Will Contest, filed on January 23, 1998, in *In re Estate of J. Howard Marshall, II*, Case No.

[2] Pursuant to Fed. R. Evid. 201, the Movant requests that this Court take judicial notice of the Complaint and to the other pleadings identified below as Exhibits.

276,815, pending in Probate Court No. 3, Harris County, Texas. With complete disregard to the increased litigation expenses for all parties and the resulting waste of judicial resources, the Debtor continues to pursue her claims in multiple settings.

The Debtor's tactics are nothing but mere forum shopping. The most recent example of the Debtor's tactics involves the Debtor's efforts to collaterally attack discovery proceedings in the Texas State Court after first participating in those proceedings. On or about June 23, 1998, the Debtor filed her Motion to Clarify or Amend Protective Order ("Motion to Amend," attached as Exhibit "D") in a case styled, *In re Estate of J. Howard Marshall II, Deceased,* pending in the Probate Court No. 3, Harris County, Texas, and under case number 276,815-402 (the "402 Case"). In her Motion to Amend, the Debtor requested that the Texas Probate Court amend a protective order (the "Protective Order," attached as Exhibit "F"), which that Court entered in January 1997 in a case styled, *Estate of J. Howard Marshall, II, Deceased, J. Howard Marshall, III v. Robert S. MacIntyre, Jr., Temporary Administrator of Estate,* Cause No. 276,815-404 (the "404 Case"). Generally, the Protective Order prohibits the parties from disseminating confidential documents to non-parties (except Court staff, employees, and attorneys of Parties, experts and fact witnesses after they execute a confidentiality agreement, etc.). The Protective Order allows *the parties* to designate documents as "confidential," and further provides a means for challenging the designation of

any document as confidential. In her Motion to Amend, the Debtor stated the following:

> Ms. Marshall requests that the Court modify the Protective Order in Case No. 276,815-404 (the "404 Case") to permit discovery products of the various Marshall related cases to be shared among the multiple claimants against the Marshall Estate. As the Court is aware, J. Howard Marshall, III, plaintiff in the '404 Case, has gathered a significant amount of evidence, particularly documentary evidence that is relevant to the determination of issues common to the cases of all claimants against the Estate of J. Howard Marshall, II.
>
> * * *
>
> The Protective Order limits disclosure to "parties," which can be read to prevent the sharing of this discovery by counsel for J. Howard Marshall, III, with non-parties to the '404 Case. Ms. Marshal [sic] believes that the Court did not intend such a narrow restriction and requests that the Court amend the protective order to permit all parties with claims to share discovery. The Protective Order should allow Marshall III and/or his counsel to share information with Ms. Marshall and other claimants as 'similarly situated plaintiffs.'

Motion to Amend at p. 2, ¶ 3.

On or about July 22, 1998, *notwithstanding her pending Motion to Amend in the Texas Court*, the

Debtor served a Notice of Subpena [sic] Duces Tecum to J. Howard Marshall, III, in the Marshall Adversary Proceeding (the "Notice," attached as Exhibit "G"). The corresponding subpoena and request for production of documents seek to compel J. Howard Marshall, III, to produce 61 categories of documents (many of these requests include numerous subparts) on August 10, 1998. In the request for production of documents (and the corresponding subpoena), the Debtor seeks various documents that are part of discovery in the Texas Probate litigation and which are clearly subject to the above-referenced Protective Order. Further, most of the requests for production of documents include a request for any and all documents in certain categories, "including documents formerly designated as 'privileged'."[3]

By issuing the subpoena to J. Howard Marshall, III, in this adversary proceeding, the Debtor continues to attempt to take advantage of the Texas Probate Court's October 17, 1997, order which has since been stayed by the Texas Supreme Court. This stayed order imposed sanctions against E. Pierce Marshall in the probate case, including a determination that various privileges asserted by Mr. Marshall and third parties had been waived. According to the Debtor, this October 1997 order somehow precludes the assertion of the attorney/client privilege in this case.

[3] This "including documents formerly designated as privileged" qualification is present Request Nos. 2, 4, 5, 8, 11-37, 39-52 and 54-58.

Mr. Marshall filed a Motion for Protective Order in the Bankruptcy Court, seeking an order directing the Debtor to first seek relief from the Protective Order in the appropriate court. Ultimately, the Probate Court (in response to a motion filed by J. Howard Marshall, III) entered an order governing J. Howard Marshall, III's production of documents he received in the Probate case. That order appears applicable in the Bankruptcy case.

D. Additional related litigation.

As noted above, Mr. Marshall's case against the Debtor originated prior to the Petition Date in this case, when the Debtor was named as a defendant in the defamation action now styled, *E. Pierce Marshall v. Diana E. Marshall, et al.*, Cause No. 95-9248J, pending in the 191st Judicial District Court, Dallas, Texas (the "Defamation Action"). After the Petition Date, Mr. Marshall dismissed (actually, "non-suited" under Texas Procedure) the Debtor from the Defamation Action and filed his dischargeability complaint against the Debtor, initiating this adversary proceeding. Diana Marshall (the remaining defendant in the Defamation Action) is an attorney retained by the Debtor in this case.

In the Defamation Action, Mr. Marshall pursued claims against Diana Marshall based on certain defamatory statements Diana Marshall made to the press and in other fora, including Diana Marshall's claims that Mr. Marshall had somehow improperly

exercised influence over the estate of his late father, J. Howard Marshall, II. Diana Marshall has described her own statements at issue in the Defamation Action as follows:

(1) A statement of Diana Marshall's legal opinion that the Debtor is entitled to one half of her husband's earning during the period of the marriage of the Debtor and J. Howard Marshall, II;

(2) The statement that what "bothers" Diana Marshall is the "blizzard of documents that were put in front of Howard Marshall to sign two weeks after his marriage to [the Debtor]";

(3) Diana Marshall's opinion that Howard Marshall's signature on such documents is "completely illegible";

(4) Diana Marshall's quoted statement that "Mr. [Howard] Marshall couldn't read at the time according to his doctors";

(5) Diana Marshall's contention that the alleged signature of J. Howard Marshall on the document giving Pierce power of attorney over the father "appears as a sort of a squiggle, with on the 'J' clearly visible";

(6) The reporter's statement that the documents "gave the son (Pierce) full control over the [sic] J. Howard Marshall";

(7) The reporter's attribution of an allegedly explanatory statement by Diana Marshall that "the effect of it was basically an attempt

to remove Howard Marshall from control of his estate;"

(8) Diana Marshall's expression of opinion that settlement of the Debtor's community property claim was possible and the "best option" for the Debtor.[4]

A review of the Debtor's counterclaim demonstrates that the defamatory statements and the challenged transactions at issue in the Defamation Action are at the heart of the Debtor's causes of action against Mr. Marshall (and third parties).

On August 16, 1998, after the trial in the Defamation Action, the jury entered a judgment against Diana Marshall and her law firm in the amount of $8.5 million. A true and correct copy of a certified copy of the Charge of the Court submitted to the jury (including the jury's findings) is attached as Exhibit

.

Thus, a party in clear privity with the Debtor (indeed, an attorney employed by the Debtor for purposes of her multi-front litigation scheme) has presented a case that is very similar to the Debtor's causes of action in this case to a fact finder. That fact finder determined the following: (1) Diana Marshall's statements regarding Mr. Marshall were slanderous

[4] *See* Exhibit "H" Response of Schecter & Marshall, L.L.P., in Opposition to E. Pierce Marshall's objections to Debtor's Application to Employ Joint Special Litigation Counsel (filed on September 11, 1996) at p. 7 (line 17) to p. 8 (line 2)

per se; (2) that Diana Marshall's statements regarding Mr. Marshall were not true or substantially true; (3) that the publication of Diana Marshall's statements in the Houston Chronicle constituted libel *per se;* and (4) that Diana Marshall made statements regarding Mr. Marshall with actual malice.[5] Based on the injury which Mr. Marshall suffered as a result of the defamatory and libelous statements by Diana Marshall, and further based upon Diana Marshall's actual malice, the jury awarded Mr. Marshall damages against Diana Marshall in the amount of $1.5 million, exemplary damages against Diana Marshall in the amount of $3 million, and exemplary damages against her law firm in the amount of $4 million.[6]

[5] *See* Exhibit 3 at pp 4-10.

[6] Mr. Marshall specifically reserves the right to renew his request that Diana Marshall and her law firm be disqualified from representation of the estate in this case. The specter of cross claims between the Debtor and Diana Marshall is now very clear (apparently, to the extent of $8.5 million). Similarly, as the Kinsella Boesch firm acts as co-counsel to the Schecter & Marshall firm in this case, Mr. Marshall reserves the right to seek disqualification of that firm as well. Finally, at the trial in the Defamation Action, Diana Marshall introduced documentary evidence which was produced in this case, and which is subject to one or more protective orders entered by this Court. Mr. Marshall reserves the right to seek sanctions against Diana Marshall for any violation of protective orders or confidentiality orders entered by this or any other Court.

III. ARGUMENT

Withdrawal of the reference is authorized by 28 U.S.C. § 157(d), which provides, "the district court may withdraw, in whole or in part, any case or proceeding referred under this section, on its own motion or on timely motion of any party, for cause shown." 28 U.S.C. § 157(d). Based on the grounds set out below, the Movant requests that this Court withdraw the reference of this Adversary Proceeding, so that the dispositive motions and trial can proceed before the District Court. As in the MPI Adversary Proceeding, discovery and other pre-trial matters can proceed before the Bankruptcy Court.

A. This Motion is timely.

Absent a showing that the non-movant is prejudiced by the timing of the filing of a motion to withdraw the reference, the request for withdrawal is not "untimely" under 28 U.S.C. 157(d). *See In re Auto Specialities Mfg. Co.,* 134 B.R. 227, 228 n.1. (W.D. Mich. 1990); *In re Texaco, Inc.,* 84 B.R. 911, 920 (S.D.N.Y. 1988); *Burger King Corp. v. B-K of Kansas, Inc.*, 64 B.R. 728, 730 (D. Kan. 1986); *Interconnect Telephone Services, Inc. v. Farren,* 59 B.R. 397, 402 (S.D.N.Y. 1986). As noted above, the parties have been engaged in a series of discovery disputes virtually since the outset of this adversary proceeding. There is no trial date set, and no dispositive motions have been filed. Depositions have barely begun. The fact that the parties have engaged in some discovery

and filed procedural motions does not render Mr. Marshall's request for withdrawal of the reference untimely. *See Burger King*, 64 B.R. at 730 (the fact that the plaintiff waited almost a year and that the parties had engaged in some discovery did not make the request for withdrawal untimely); *Interconnect*, 59 B.R. at 402 (the fact that the movent waited one year, the parties conducted discovery, and that the movants unsuccessfully moved to dismiss the complaint did not render the request for withdrawal of the reference untimely). Simply put, based on the procedural posture of this case, the Debtor cannot establish that her pre-trial preparation has "proceeded to such an extent that a withdrawal motion would result in any prejudice." *See In re Texaco, Inc.*, 84 B.R. at 920. Accordingly, Mr. Marshall has timely presented his request for withdrawal of the reference in this action.

B. Based on the nature of Mr. Marshall's Complaint, the Bankruptcy Court cannot consider the merits of this action.

The Bankruptcy Court is jurisdictionally infirm to determine the underlying personal injury tort claim which Mr. Marshall asserts in this adversary proceeding. In pertinent part, 28 U.S.C. § 157 provides as follows:

> The district court shall order that personal injury tort and wrongful death claims shall be tried in the district court in which the bankruptcy case is pending, or in the district

> court in the district in which the claim arose, as determined by the district court in which the bankruptcy case is pending.

28 U.S.C. § 157(b)(5).

Torts of libel, slander and the like are acts committed against the person and constitute personal injury torts under Texas state law. *See Brewster v. Baker,* 139 S.W.2d 643, 644 (Tex. Civ. App. – Beaumont 1940, no writ) ("Damage to character as the result of slander or libel is a "personal injury."). Similarly, Bankruptcy Courts have recognized that defamation claims are "personal injury tort claims" for purposes of 28 U.S.C. § 157(b)(5). *See, e.g., In re Boyer*, 93 B.R. 313, 317 (Bankr. N.D.N.Y. 1988) (applying 28 U.S.C. § 157(b)(5), and citing Black's Law Dictionary, the court stated "The term 'personal injury tort' embraces a broad category of private or civil wrongs or injuries for which a court provides a remedy in the form of an action for damages, and includes damages to an individual's person and any invasion of person rights, *such as libel, slander* and metal suffering[.]" [italics added]).

Mr. Marshall's Dischargeability Complaint against the Debtor is a routine "core" bankruptcy matter. However, the underlying claim which Mr. Marshall asserts to be non-dischargeable: (i) has been contested by the Debtor; (ii) has never been determined by a Court (except collaterally by the Texas state court); and (iii) is for a personal injury tort

claim under Texas state law. Thus, the Complaint *must* be heard by this Court (or abstained from).

C. Alternatively, factors deemed relevant by the Ninth Circuit militate in favor of discretionary withdraw of the reference.

In determining whether withdrawal of the reference under 28 U.S.C. section 157(d) is appropriate, the District Court must first evaluate whether the proceeding is a core or non-core matter under 28 U.S.C. § 157(b). *See Orion Pictures Corp. v. Showtime Networks, Inc. (In re Orion Pictures Corp.),* 4 F.3d 1095, 1101 (2d Cir. 1993) (cited favorably by the Ninth Circuit in *Security Farms v. Int'l Brotherhood of Teamsters, Chauffeurs, Warehousemen & Helpers,* 124 F.3d 999 (9th Cir. 1997)). After making this determination, the Court must next consider the propriety of withdrawal under the standards developed by federal courts. *Id.*

Only the Debtor's first cause of action appears to fall within the specific examples of "core matters" set out in 28 U.S.C. § 157(b)(2)(B)-(N). The remaining causes of action set out in the Counterclaim do not fall within the specific core matters identified in those

subsections or in the "catch all" provisions of 28 U.S.C. § 152(b)(2)(A) and (O).[7]

Notwithstanding the apparent absence of core issues in this adversary proceeding, this Court need not consider this issue in determining whether withdrawal of the reference is appropriate. As this Court determined in the MPI Adversary Proceeding, sufficient independent grounds exist for withdrawal of the reference, notwithstanding a core versus non-core determination regarding the causes of action the Debtor asserts in the Counterclaims. *See* MPI Withdrawal Order at pp. 4-9.

In determining whether a movant has established sufficient "cause" for withdrawal of a reference, the Ninth Circuit has held that District Courts should consider the following factors: (a) the efficient use of judicial resources; (b) delay and cost to the parties; (c) uniform bankruptcy administration; (d) the reduction of forum shopping; and (e) other related factors. *See, e.g., Security Farms*, 124 F.3d at 1008. As is demonstrated below, consideration of these factors militates heavily in favor of withdrawal of the reference of this Adversary Proceeding.

[7] According to the Ninth Circuit, proceedings that do not invoke a substantive right created by federal bankruptcy law, but instead involve only rights which could exist outside the bankruptcy context, are not core proceedings. *Security Farms*, 124 F.3d at 1008; *Eastport Assocs v. City of Los Angeles (In re Eastport Assocs.)*, 935 F.2d 1071, 1076 (9th Cir. 1991).

1. "Other factors" predominate in this case – primarily, the risk of inconsistent judgments in the corresponding adversary proceedings.

As noted above, the Debtor has alleged the identical causes of action against different defendants in this adversary proceeding and in the MPI Adversary Proceeding. One of these cases will be tried before the Bankruptcy Court, while the other is tried before the District Court on presumably separate procedural schedules. The possibility of inconsistent judgments in the two cases clearly exists. Further, there is a danger that a judgment in one case could have preclusive effect on litigants in the other case. These dangers would be cured by withdrawal of the reference and the subsequent consolidation of the two cases.

2. Withdrawal of the reference will promote the efficient use of judicial resources.

As noted above, the Debtor has filed virtually the identical complaint against the Movant and against the other defendants in the two adversary proceedings. Based on the current procedural posture of the two cases, there will be a trial in this Court and in the Bankruptcy Court regarding the identical facts and disputes. This situation is inherently wastful of judicial resources. Withdrawal of the reference will undoubtedly result in an economic use of court time.

3. Withdrawal of the reference will not cause undue expenditure of the Debtor's resources.

The expenses associated with this litigation will not increase unreasonably if dispositive motions and trial are handled by the District Court. In fact, by virtue of the fact that the parties will prepare or defend dispositive motions and prepare for trial in *one* Court, the Debtor will likely benefit from withdrawal of the reference. Further, as this Court has previously observed, allowing the Bankruptcy Court to administer pre-trial matters will best conserve the parties' resources. *See* MPI Withdrawal Order at p. 8.

4. Withdrawal of the reference will not impinge upon uniform bankruptcy administration.

Except to the extent that the Debtor apparently hopes to fund any plan of reorganization out of the proceeds of this of [sic] litigation, this Adversary Proceeding does not relate to the Debtor's underlying bankruptcy case. The Debtor's main bankruptcy case will not be affected in any manner by the withdrawal of the reference. To the extent that this case affects the main case, this Court has previously recognized that any impact is minimized by allowing the Bankruptcy Court to manage discovery and other pre-trial matters. *Id.*

5. Withdrawal will not encourage forum shopping.

The Movant is not engaging in forum shopping in this case. As noted above, there is a clear danger of

inconsistent judgments in this case. Further, the prospect of two trials regarding the Debtor's causes of action simply does not make economic or procedural sense. Withdrawal of the reference in this case is clearly appropriate.

IV. CONCLUSION

E. Pierce Marshall respectfully requests that this Court withdraw the reference of this Adversary Proceeding and grant him any other relief as is just.

Respectfully submitted this 22nd day of September, 1998.

VERNER, LIIPFERT, BERNHARD,
MCPHERSON & HAND CHARTERED

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Attorneys for Debtor and Plaintiff
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UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

In Re:	) Case No. CV 98-7686 WDK
VICKIE LYNN MARSHALL,	) Bk. Case No. LA 96-12510-SB) Adv. No. 96-01838
Debtor.	) Chapter 11
E. Pierce Marshall,	) **DEBTOR VICKIE LYNN MARSHALL'S NOTICE**
Plaintiff,	) **OF LODGING RE OPPO-**
v.	) **SITION OF DEBTOR TO**
Vickie Lynn Marshall,	) **MOTION OF E. PIERCE MARSHALL FOR WITH-**
Defendant.	) **DRAWAL OF REFER-**
	) **ENCE OF ADVERSARY**
	) **PROCEEDING**

Vickie Lynn Marshall, Counterclaimant, v. E. Pierce Marshall, Counterdefendant.	)	DATE: October 19, 1998 TIME: 1:00 p.m. CTRM: 312 N. Spring St. Los Angeles, CA 90012

Attached hereto as Exhibit 1 is a true and correct copy of a document entitled Order Re Discovery Sanctions Against E. Pierce Marshall, which Order was entered by the Bankruptcy Court on October 13, 1998. This Order, which among other things sanctions Plaintiff E. Pierce Marshall ("Pierce") $25,000, lends further support to Debtor Vickie Lynn Marshall's Opposition to Pierce's Motion to Withdraw the Reference. Namely, the Order provides plain evidence as to the reason why Pierce has moved only now to withdraw the reference, two full years after he brought his Complaint for Nondischargeability in this bankruptcy proceeding.

Simply put, Pierce apparently realizes that he can no longer delay and obstruct discovery in this matter without penalty from the Bankruptcy Court. That is why Pierce now brings his untimely motion; he "forum shops" in the hope that by bringing this case before a new Court unfamiliar with Pierce's pattern of discovery abuse, the Bankruptcy Court's authority in supervising this proceeding will be undercut. Debtor thus reiterates her opposition to Pierce's untimely motion to withdraw the reference.

DATED: October 15, 1998

KINSELLA, BOESCH,
FUJIKAWA & TOWLE, LLP

By: /s/ Joshua A. Meyer
JOSHUA A. MEYER
Attorneys for Debtor
VICKIE LYNN MARSHALL

EXHIBIT 1

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UNITED STATES BANKRUPTCY COURT

CENTRAL DISTRICT OF CALIFORNIA

In re VICKIE LYNN MARSHALL, Debtor. E. Pierce Marshall, Plaintiff, v. Vickie Lynn Marshall, Defendant. and related Counter-claims.	CASE NO. LA 96-12510 SB Chapter 11 Adversary No. 96-01838 **[PROPOSED] ORDER RE DISCOVERY SANCTIONS AGAINST E. PIERCE MARSHALL** (Filed Oct. 9, 1998)

The motion of Debtor Vickie Lynn Marshall ("Debtor") for an order for sanctions against Plaintiff E. Pierce Marshall came on regularly for hearing on August 27, 1998, before the Honorable Samuel L. Bufford. Having considered the papers filed in support of and in opposition to the motion, the arguments presented at the hearing on the motion, and good cause appearing, the Court orders as follows:

1. No later than September 26, 1998, Pierce Marshall shall pay sanctions in the amount of $25,000.00 by delivery of a check payable to Kinsella, Boesch, Fujikawa & Towle.

2. Debtor shall prepare a written comparison of the of the [sic] documents appearing on the privilege logs submitted by the law firm of Hunter, Blazier, O'Dowd & Moreno in August, 1998 (three privilege logs were submitted bearing the dated [sic] August 4th, August 10th and August 11th), which documents do not appear on earlier logs. The comparison shall be filed with the Court and served on Pierce on or before September 10, 1998. Pierce Marshall shall file and serve a reply to Debtor's written comparison on or before September 21, 1998. All service shall be by personal service or overnight delivery.

3. A further hearing on Debtor's motion for sanctions will be held on October 29, 1998 at 2:00 p.m. in Courtroom 1575 of the Roybal Building, 255 E. Temple Street, Los Angeles, California, 90012.

IT IS SO ORDERED.

Dated:
OCT -9 1998

/s/ SAMUEL BUFFORD
THE HONORABLE
SAMUEL L. BUFFORD
U.S. Bankruptcy Court Judge

ER-2043

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

CIVIL MINUTES – GENERAL

Case No. CV 98-7686-WDK

Date: October 21, 1998

Title: Marshall v. Marshall

DOCKET ENTRY

PRESENT:

The Honorable William D. Keller, Judge

Amalia Carrillo	None Present
Courtroom Deputy Clerk	**Court Reporter**

ATTORNEYS PRESENT FOR PLAINTIFFS:

None Present

ATTORNEYS PRESENT FOR DEFENDANTS:

None Present

PROCEEDINGS:

Plaintiff E. Pierce Marshall's motion to withdraw the reference is granted, in part:

(1) Debtor's Chapter 11 petition remains before the bankruptcy court;

(2) Plaintiff E. Pierce Marshall's claim for dischargeability of debt remains before the bankruptcy court;

(3) The claim of defamation raised by plaintiff E. Pierce Marshall (hereinafter E.P.M.) remains before the bankruptcy court only to the extent it pertains to the issue of dischargeability of debt;

(4) The underlying suit for defamation is withdrawn to this Court;

(5) Debtor's counterclaim against E.P.M. is withdrawn to this Court and consolidated with the "MPI proceeding" (CV-98-4398-WDK);

(6) All discovery matters currently pending in the bankruptcy court shall proceed before the bankruptcy court; and

(7) All discovery matters which the bankruptcy judge determines are necessary to the "core" bankruptcy proceedings (debtor's Chapter 11 petition and E.P.M.'s claim for dischargeability of debt) shall proceed before the bankruptcy court.

IT IS SO ORDERED.

Initials of Courtroom Deputy Clerk AC

SER-6180-6190

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

- - - - - -

THE HONORABLE WILLIAM D. KELLER,
UNITED STATES DISTRICT JUDGE

E. PIERCE MARSHALL, PLAINTIFF,	)	
VS.	)	CV 98-7686-WDK
VICKIE LYNN MARSHALL, DEFENDANT.	)	

REPORTER'S TRANSCRIPT OF PROCEEDINGS

LOS ANGELES, CALIFORNIA

TUESDAY, MARCH 9, 1999

PLAINTIFF'S MOTIONS

DEBORAH K. GACKLE, CSR, RPR
Official Court Reporter
U.S. District Court
312 North Spring Street
Room 402-A
Los Angeles, CA 90012
(213) 620-1149

* * *

[3] LOS ANGELES, CALIFORNIA;
TUESDAY, MARCH 9, 1998; 10:50 A.M.

THE COURT: Gentlemen, good morning. Be seated, please.

I note the hour. I spent the time this morning trying to recreate what's happened here, and it's a tortured trail; and, frankly, it's a combination of factors that have contributed to this. If the parties were working with good will, they could have resolved it amongst themselves; but for various and sundry purposes, it's my belief, for advantage, they have taken different positions.

As I understand the lawsuit, when it initially arrived in this courthouse, it was Vickie Marshall who was seeking some kind of bankruptcy protection. And it was Pierce Marshall who really started the problem by saying, "Hey, you can't discharge my defamation claim," okay?

You know, Pierce Marshall, stay back in Texas and take care of it there, okay? But, no, you had to come here, and you come here and you start this fire fight, all right? All right.

So once Pierce decide [sic] to come her [sic] the bankruptcy court you got Vickie failing out [sic] say I will see [sic] you if you sue me.

Vickie proceeds to sue, and she sues just about everybody in sight, to include the oil company that

the late Howard Marshall, J. Howard, was involved with. And she sues

* * *

[67] He orders them to – "You have them in your possession, custody and control, Mr. Melko?"

"Yes, I do."

"You won't bring them to me, you're ordered to, you don't?"

"No."

I mean, you know, it's – there's a pretty measured step here, but there is court recognition in the findings that's just defiance.

I mean, when – I'll tell you what, if Your Honor ordered me to bring a box of documents to the court, I'd bring a box of documents to the court, especially if I'm facing death penalty sanctions, motions, and I've been through seven hearings on them, and I got a court who's warned me seven times, I'd listen. But at some point here, Your Honor, this is about respect for federal court orders.

Your Honor, your October 21 order was crystal clear. There is no evidence that Judge Bufford violated that on February 2 or at any other time.

THE COURT: I don't believe he did violate the order, but what I am concerned about is this last increment of sanctions which are in the extreme.

And it may be that they're warranted, but I'm asked to review them and to make a meaningful decision in a mandamus setting, which is an extreme setting.

* * *

[86] don't – I can't –

THE COURT: Sanction-wise I'm talking about.

MR. MELKO: Well, we don't think any – I think I can prove to you the sanctions aren't warranted, but I don't know, besides money and what they've asked for, which is striking defenses, I'm not sure what other sanctions are available.

THE COURT: Thank you.

I am going to call the bankruptcy judge about the management of the case. And my present inclination is to make something akin to a Solomonic cut, which is to say there will be no death penalty sanctions vacated on the record that's before me and – because of the impact on third party. I'm going to reinstate the – I'm going to lift the stay on the 25 and the 15, and I'm going to refer everything to the bankruptcy judge, with the exception of MPI and Ferrar, which will be stayed pending the outcome of Texas and the bankruptcy case.

And if you can convince the bankruptcy judge to stay pending Texas, which would be my inclination, but I'm not as deeply into it from a bankruptcy

standpoint as the bankruptcy judge is, certainly that would be the way I would proceed were the case in this court.

But, practically speaking, given where you are now, I can't try this case. Bankruptcy judge can. He knows what's going on. And as far as the memorandum that he shared with me, he does have the authority to try everything but the MPI case, [87] as far as I can tell. So I could vacate the withdrawal order under 157, vacate the withdrawal, send you back to bankruptcy court and have this tried in toto, with the exception of MPI – or – yes, MPI, unless you convince him that there should be a stay of the Texas proceeding.

I further tell you that I will not honor any sanction order in this court on review henceforth, unless it is thoroughly documented. So whoever obtains a sanction order, if indeed it is obtained, I want a rendition of the merits. In other words, for instance, when the bankruptcy judge comes to me with a death penalty sanction and says – which may be known to him, but it is not to me – for instance, No. 3, page 2 of his order, "Despite this Court's order, he – " that's Pierce, and I'm excerpting – "refused to produce many documents in his custody or control."

I want some specification. No. 4, he's saying "Those documents – " "failed to produce those documents to the plan." I want some specification. And if there's any dollar sanction, I want the specification.

You may want to beef that up in the record, Mr. Boesch. I'm not saying you won't get it, because I've got the sense that they have been stonewalling and unless it's clearly erronative, his order is going to stand. And my preliminary – underscore preliminary – ruling is that he's correct. But I want – if you ever come back here on this, I want something other than [88] your claiming 50 and him giving 25. You got to have more. Can't do under that Yagman case. Plus, common sense tells you you can't do it.

So I may not even liaison with him. I just may say that this is – finalize this order. I know it's not determinative, but the fact of the matter is E. Pierce Marshall implicated the jurisdiction of that bankruptcy court. He chose to be a party to that litigation. And much of what we see here is the spawn of what he begot, okay? Absolutely.

You know, she didn't – Vickie Marshall didn't include him in this litigation. He wanted to be included, and he has found himself included as a consequence.

(Discussion held off the record.)

THE COURT: I am going to finalize the order. That is the order.

One, the matter is – any matters withdrawn, save Marshall Petroleum – it's Vickie Marshall's suit against Marshall Petroleum, et al., as I recall it, is – I vacate the withdrawal order. Okay. Return to the bankruptcy court where you will stay.

This is driven part by your selection of forum by E. Pierce Marshall, part by judicial economy reasons, and part by my inability to see this matter to conclusion, and part by the immersion that the bankruptcy judge has in this case.

Associated with that ruling, if the bankruptcy Court [89] wishes to stay in deference to the Texas proceeding, that is up to the bankruptcy court. That is the first ruling. Number two, as regards the petition for mandamus, denied on one and two, sections one and two, the 25 and 15, because you have not met the very high Bauman standard – B-a-u-m-a-n. And I don't need – I don't think I need to go all the various permeations of the consideration, but you do have other means, such as appeal, to obtain desired relief. If there is damage, it's correctable on appeal.

The district court order, that is, the bankruptcy court order, is not clearly erroneous as a matter of law. There is no manifestation of oft-repeated error or persistent disregard of the federal rules by the bankruptcy court. And there are no new important problems or issues of first impression. That holds true for both the 25 and the 15.

THE WITNESS: However – and associated with that, the one and two denying mandamus, I lift the stay on one and two. I don't, frankly, think there was ever, effectively, a one stay; but one and two is lifted.

And payment is due – how much time, Mr. – he is going to have to determine, not me. Leave it to the bankruptcy judge to figure that out.

Then as regards sanction No. 3, what we've been referring to as the death penalty sanctions, I don't think there is sufficient record here, albeit – I say this to you, [90] Mr. Boesch, and I say this to the bankruptcy court, based on what I've seen: I commiserate with both of you, all right? But I don't think there's a sufficient enough record to warrant death penalty sanctions. I don't think they're as measured as they could be. If you wanted more, something as aggressive as this, you had to submit something that was more specific. You didn't and the bankruptcy judge didn't; therefore, given the very significant impact on a number of third parties and given the very escalated nature of this penalty sanction, I think that this is the unusual case where mandamus is appropriate. I'm vacating the sanction order.

Now, I say to you if there are going further sanction orders, document them, okay? You prepare the order for the bankruptcy judge if it's appropriate. And if you have it documented by the bankruptcy judge, then come back here and excerpt your record. Don't go giving me these piles of documents here, both sides.

I do believe that – and I've ordered the stay of the Vickie Marshall versus MPI, Marshall Petroleum, Inc., case. What else, if anything, remains unaddressed?

MR. CAINE: Your Honor, I just did want to make that clear, because the first part – I represent Marshall Petroleum.

So all matters are stayed with respect to that pending the determination of the probate court; is that correct?

THE COURT: Only the Marshall Petroleum case.

[91] MR. CAINE: Yes.

THE COURT: Or given further application by Vickie Marshall after any proceedings that may be undertaken in front of the bankruptcy court. In other words, you got some more input, Mr. Boesch, come back. Right now, I don't see it.

MR. CAINE: Thank you.

THE COURT: Anything else needs to be addressed?

Okay. I'm sorry you had to wait so long, but you know that there was a lot to review here.

MR. BOESCH: By way of inquiry, is Your Honor's statement from the bench to be taken as the order, as opposed to a subsequent written order?

THE COURT: You want to prepare an order, fine. Other than that, you're going to get a minute order, and that's it. I'm not proposing an order. You want to give me an order – I think this is fairly explicit. I probably thought my 10-21-98 order

was fairly explicit. But I do believe this covers the basis that you wanted covered. May not be that you got all the relief you wanted, but you have considerable relief, I'll tell you, because you're in that bankruptcy court getting this resolved. And he is somebody who understands what is afoot.

So judging by what you have here, he understands who he's dealing with, and if you don't get responses from them then – let me say this. Don't be overly imbued by this ruling. Somebody was just executed, literally, in the state of [92] California. Last execution I ordered, okay? That gives you an idea of what could what [sic] of happen in a civil case. I'm not looking for it, and I wasn't looking for that man who murdered two people in grizzly murders either. But, if necessary, I will order it. Probably couldn't be better example than that case.

So if you have a problem with them where they stonewall you, you have this record, they have had more than enough warning, and I'm telling you, Mr. Boesch, and I'm telling them through you, I will not hesitate to terminate, effectively, this lawsuit if you stonewall him improperly.

So if I were you gentlemen, I wouldn't give the bankruptcy court any problems because don't think you're going to come back to me as a safety valve. All they have to do, that is the plaintiff, is document things; and if it's documented and it's warranted, you will get the ultimate sanction. I'm not looking for it,

but I'll do it. Don't be emboldened. I'll leave you with that, okay? Thank you.

If any party believes the minute order that emanates from there [sic] court is at all confusing – I'm hopeful it is not – I want to hear from you, okay? The clerk is going to do it now, the law clerk.

(Proceedings concluded at 3:50 p.m.)

[Certification Omitted In Printing]

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

THE HONORABLE WILLIAM D. KELLER,
UNITED STATES DISTRICT JUDGE

E. PIERCE MARSHALL,	)	
PLAINTIFF,	)	
VS.	)	CV 98-7686-WDK
VICKIE LYNN MARSHALL,	)	
DEFENDANT.	)	

REPORTER'S TRANSCRIPT OP PROCEEDINGS

LOS ANGELES, CALIFORNIA

TUESDAY, MARCH 9, 1999

PLAINTIFF'S MOTIONS

DEBORAH K. GACKLE, CSR, RPR
Official Court Reporter
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312 North Spring Street
Room 402-A
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(213) 620-1149

* * *

[88] THE COURT: I am going to finalize the order. That is the order.

One, the matter is – any matters withdrawn, save Marshall Petroleum – it's Vickie Marshall's suit against Marshall Petroleum, et al., as I recall it, is – I vacate the withdrawal order. Okay. Return to the bankruptcy court where you will stay.

This is driven part by your selection of forum by E. Pierce Marshall, part by judicial economy reasons, and part by my inability to see this matter to conclusion, and part by the immersion that the bankruptcy judge has in this case.

Associated with that ruling, if the bankruptcy Court [89] wishes to stay in deference to the Texas proceeding, that is up to the bankruptcy court. That is the first ruling. Number two, as regards the petition for mandamus, denied on one and two, sections one and two, the 25 and 15, because you have not met the very high Bauman standard – B-a-u-m-a-n. And I don't need – I don't think I need to go all the various permeations of the consideration, but you do have other means, such as appeal, to obtain desired relief. If there is damage, it's correctable on appeal.

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* * *

SER-6717-6718

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

CIVIL MINUTES - GENERAL

Case No. CV 98-7686-WDK

Date: March 10, 1999

Title: *In re Vickie Lynn Marshall; E. Pierce Marshall v. Vickie Lynn Marshall; Vickie Lynn Marshall v. E. Pierce Marshall*

DOCKET ENTRY

PRESENT:

The Honorable William D. Keller, Judge

Amalia Carrillo	None Present
Courtroom Deputy Clerk	**Court Reporter**

ATTORNEYS PRESENT FOR PLAINTIFFS:

None Present

ATTORNEYS PRESENT FOR DEFENDANTS:

None Present

PROCEEDINGS:

The Court orders the following:

(1) This Court's October 21, 1998 Order is vacated. Accordingly, Case No. CV 98-7686,

In re Vickie Lynn Marshall, is referred back to the Bankruptcy Court,

(2) The reference in Case No. CV 98-4398-WDK, *Vickie Lynn Marshall v. Finley Hilliard, et al.*, remains withdrawn to this Court. However, this case is stayed, pending resolution of either the proceeding in Texas Probate Court or the resolution of CV 98-7686, *In re Vickie Lynn Marshall* before the Bankruptcy Court;

(3) E. Pierce Marshall's petition for a writ of mandamus vacating the Bankruptcy Court's sanction order of $25,000, entered on October 13, 1998, is denied.

(4) E. Pierce Marshall's petition for a writ of mandamus vacating the Bankruptcy Court's sanction order of $15,000, entered on January 22, 1999, is denied;

(5) The order staying the payment of monetary sanctions, issued by this Court on February 1, 1999, is lifted;

(6) E. Pierce Marshall's petition for a writ of mandamus vacating the Bankruptcy Court's sanction order issuing "terminating sanctions," entered on February 2, 1999, is granted. The Bankruptcy Court's sanction order, entered on February 2, 1999 is vacated.

IT IS SO ORDERED.

PETITIONER'S BRIEF

Supreme Court, U.S.
FILED
NOV 12 2010
OFFICE OF THE CLERK

No. 10-179

In The Supreme Court of the United States

HOWARD K. STERN, EXECUTOR OF THE ESTATE OF VICKIE LYNN MARSHALL,

Petitioner,

v.

ELAINE T. MARSHALL, EXECUTRIX OF THE ESTATE OF E. PIERCE MARSHALL,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

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540

QUESTIONS PRESENTED

In the 1984 Bankruptcy Act, Congress divided bankruptcy court jurisdiction into "core" proceedings, in which bankruptcy judges can enter final orders, and "non-core" proceedings that are subject to district court de novo review. *See* 28 U.S.C. §157(b). Congress expressly identified certain core proceedings, including "counterclaims by the estate against persons filing claims against the estate." §157(b)(2)(C). Despite Article III challenges, lower courts across the country have uniformly held for decades that bankruptcy courts can enter final orders on debtors' compulsory counterclaims to proofs of claim.[1] Until now.

The Ninth Circuit opinion here holds that under *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982) (*Marathon*) and *Katchen v. Landy*, 382 U.S. 323 (1966), core jurisdiction constitutionally exists under §157(b)(2)(C) only for compulsory counterclaims entirely encompassed within the allowance or disallowance of the creditor's claim against the estate and that raise no issue beyond that claim. Even though here the debtor's compulsory counterclaim constituted an affirmative defense to

[1] A debtor's compulsory counterclaim to a proof of claim is any counterclaim that, at the time of pleading, arises out of the same transaction or occurrence as the creditor's claim against the estate and is not already pending in another action. Fed. R. Bankr. P. 7013; Fed. R. Civ. P. 13(a).

QUESTION PRESENTED – Continued

the proof of claim and, if decided first, would have defeated it entirely, the Court held the counterclaim was non-core because the debtor had to prove additional elements to prevail on it.

Accordingly, the questions presented are:

1. Whether the Ninth Circuit opinion, which renders §157(b)(2)(C) surplusage in light of §157(b)(2)(B), contravenes Congress' intent in enacting §157(b)(2)(C).

2. Whether Congress may, under Articles I and III, constitutionally authorize core jurisdiction over debtors' compulsory counterclaims to proofs of claim.

3. Whether the Ninth Circuit misapplied *Marathon* and *Katchen* and contravened this Court's post-*Marathon* precedent, creating a circuit split in the process, by holding that Congress cannot constitutionally authorize non-Article III bankruptcy judges to enter final judgment on all compulsory counterclaims to proofs of claim.

PARTIES TO THE PROCEEDING

The original parties to this case, Vickie Lynn Marshall and Pierce Marshall, died during the pendency of this appeal. The current parties are Howard K. Stern, Executor of the Estate of Vickie Lynn Marshall, and Elaine T. Marshall, Executrix of the Estate of E. Pierce Marshall.

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MISCELLANEOUS

1 Alan N. Resnick & Henry J. Sommer, Collier on Bankruptcy (16th ed. 2010) 18, 28, 29

10 Alan N. Resnick & Henry J. Sommer, Collier on Bankruptcy (15th ed. 2010) 28

OPINIONS BELOW

The Ninth Circuit's opinion is reported at 600 F.3d 1037 (9th Cir. 2010), Appendix to the Petition for a Writ of Certiorari ("App.") at 1-89.

Three opinions of the District Court for the Central District of California are reported at 275 B.R. 5 (C.D. Cal. 2002), App. 90-214; 271 B.R. 858 (C.D. Cal. 2001), App. 217-34; and 264 B.R. 609 (C.D. Cal. 2001), App. 239-85. A fourth is unpublished, App. 235-38.

Two opinions of the Bankruptcy Court for the Central District of California are reported at 257 B.R. 35 (Bankr. C.D. Cal. 2000), App. 286-99; and 253 B.R. 550 (Bankr. C.D. Cal. 2000), App. 313-36. A third is unpublished, App. 305-12.

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JURISDICTION

The Ninth Circuit issued its opinion on March 19, 2010; it denied panel and *en banc* rehearing on May 5, 2010. App. 1, 337-38.

This Court has jurisdiction under 28 U.S.C. §1254(1). Jurisdiction was proper in the District Court under 28 U.S.C. §§1331 and 1334, and in the Ninth Circuit under 28 U.S.C. §1291.

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CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

Relevant portions of Article I, § 8, and the entirety of Article III of the United States Constitution are reprinted at App. 339-41.

28 U.S.C. §§157 ("§157"), 1331 and 1334 are reprinted at App. 342-47.

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STATEMENT OF THE CASE

Both the bankruptcy and district courts below found that Vickie's[2] husband J. Howard Marshall, II ("Howard") attempted to provide for Vickie through an inter vivos trust. App. 25-26, 134-48, 198-202. Those courts concluded that his son Pierce suppressed or destroyed the trust instrument and stripped Howard of his assets before his death. App. 25-26, 143-202, 211-14. The bankruptcy and district courts found Pierce liable for tortious interference and awarded Vickie millions in compensatory and punitive damages. App. 3, 214.

A. The Bankruptcy Proceedings.

In January 1996, Vickie sought Chapter 11 bankruptcy protection following Howard's death.

[2] For the sake of readability, we adopt the Ninth Circuit's approach and refer to the petitioner as Vickie Lynn Marshall ("Vickie") and the respondent as Pierce Marshall ("Pierce").

App. 91-93. Pierce, after stating his unequivocal intention to file "proofs of claims that provide us the maximum range of options" in the "VLS bankruptcy," Joint Appendix ("JA") 55, dismissed a pending state-court defamation suit against Vickie and brought his defamation claims into the bankruptcy court by filing, in May 1996, a nondischargeability complaint to pursue claims against Vickie personally, and, in June 1996, a separate proof of claim for an unliquidated amount of damages against Vickie's bankruptcy estate. App. 14-16 nn.10 & 11, 77-87, 266-67 n.17, 274-76; JA 57, 59, 105; Supplemental Excerpts of Record ("SER") 6101-02, 6801 (Pierce telling bankruptcy court that the amount of his creditor's claim "shall be determined by the adversary proceedings filed herein" and he is "happy" to litigate "[his] claim here" because "we did choose this forum"); *see* SER 8409-19 (Pierce requesting from the bankruptcy court an $8.5 million estimation of his claim for plan confirmation and voting purposes).

Vickie objected to Pierce's proof of claim, answered his adversary complaint pleading truth as an affirmative defense, and filed a compulsory counterclaim for tortious interference with an inter vivos gift. App. 15-16, 48 n.29, 94, 378-81; SER 12204. This was the first time Vickie asserted that claim in any court. App. 48 n.29; JA 84; *In re Marshall*, 273 B.R. 822, 825-26 (Bankr. C.D. Cal. 2002); SER 12260.

Shortly after Vickie filed her counterclaim, the bankruptcy court found that it was compulsory as it arose out of the same transactions and occurrences as

Pierce's proof of claim and that it was core under subsections (B) and (C) of §157(b)(2), which includes as core proceedings, respectively, "allowance or disallowance of claims against the estate" and "counterclaims by the estate against persons filing claims against the estate." App. 294-96, 306-07.[3]

More than two years after filing his proof of claim, and faced with the imminent prospect of monetary and terminating sanctions by the bankruptcy court, Pierce moved for the first time to withdraw the reference of the adversary proceeding "so that the case will proceed before the District Court for purposes of the mandatory status conference, dispositive motions and trial." JA 95, 128-29; Excerpts of Record ("ER") 1949-57; SER 8697, 8703-10.[4]

[3] Pierce acknowledged that "the defamatory statements and the challenged transactions" that were at issue in his dismissed state-court defamation action and carried over into his proof of claim "are at the heart of" Vickie's counterclaim. JA 107. And he told the bankruptcy court that his defamation claim and Vickie's counterclaim constituted "both halves" of the same action. App. 275.

[4] After the close of pleadings, Pierce unsuccessfully filed motions in the bankruptcy court to stay Vickie's counterclaims, to dismiss her counterclaims and, belatedly, in January 1997, for abstention. ER 957, 1049; SER 6111, 6114, 6122, 6748, 8596-97. In addition, there was pervasive judicial activity in the bankruptcy court regarding Pierce's resistance to discovery, including his failure to produce critical documents, his admitted destruction of potentially relevant documents after Vickie's requested production, his failure to appear for depositions (at least once in direct violation of a court order), and his failure to pay discovery sanctions. *See* ER 1949-57; SER 8697, 8703-10.

The district court initially granted Pierce's motion, ordering the defamation claim and Vickie's compulsory counterclaim "withdrawn to this Court." JA 122-23. However, it vacated its initial order and referred the case back to the bankruptcy court. JA 129, 138-39. It explained that its decision was driven by Pierce's "selection of forum," stressing that Vickie did not include Pierce in the litigation, that Pierce "wanted to be included" and that "much of what we see here is the spawn of what he begot." JA 129-30. The court also mentioned, inter alia, "judicial economy reasons" and "the immersion the bankruptcy judge has in this case." JA 130.

Trial began in the bankruptcy court in late 1999. During trial, the court granted Vickie's pending motion for summary judgment on Pierce's defamation claim on the ground that Vickie neither published nor ratified the alleged defamatory statements, App. 18, 244-45, a decision Pierce never appealed. After a full trial, the bankruptcy court found Pierce liable for tortious interference with a gift and awarded compensatory damages of $449 million (the amount of the intended trust) and $25 million in punitive damages, entering judgment in December 2000. App. 18-20, 286-336.[5] Under Vickie's bankruptcy plan, the counterclaim proceeds are to be applied first to creditor claims. App. 17; SER 6074-75.

[5] The judgment was based partly on evidentiary sanctions, the court having found that Pierce engaged in "massive discovery abuse," including destroying documents relevant to Vickie's claim. App. 19-20 n.17, 317 n.5, 320-26.

B. The Texas Probate Proceedings.

A Texas probate court began administering Howard's estate in August 1995. App. 11. Vickie first appeared in that proceeding in 1998, when she joined a pending will contest filed by Pierce's brother. App. 12, 48 n.29. In January 2000, Vickie prophylactically filed her tortious interference with gift claim in the probate court after Pierce argued that the bankruptcy court lacked jurisdiction under the probate exception. *Marshall*, 273 B.R. at 825-26; SER 12260.

After the bankruptcy court entered judgment for Vickie in December 2000, Vickie immediately filed the bankruptcy judgment in the Texas probate court and voluntarily nonsuited her claims there without prejudice. App. 20, 232; *Marshall*, 273 B.R. at 826; SER 8426-27, 10306.

After nonsuiting her claims, Vickie at first remained in the probate proceedings only as a counter-defendant on a sanctions claim Pierce had brought in 1999. App. 21 & n.18, 223 n.4; SER 8422-27. Pierce then brought new claims against Vickie in an effort to re-litigate the issues the bankruptcy court had already decided. *Marshall*, 273 B.R. at 825-26; SER 8427-28, 8606-28, 12260-61.

Although the bankruptcy court directed Pierce to dismiss all his new probate claims, *Marshall*, 273 B.R. at 826, 831; SER 8431-33, Pierce's attorneys dismissed only a tortious interference claim, assuring the bankruptcy court that any risk of inconsistent judgments had been eliminated, that the "only" issue

in the probate-court trial "directed at Ms. Marshall" was whether Howard and Vickie had an agreement for him to give her one-half his property and that, in seeking declaratory relief and submitting that issue, Pierce "only seek[s] to avoid any possibility of future litigation with Vickie Marshall over [Howard's estate] and to ensure that the Texas Probate Court can determine all claimants and efficiently administer that estate," ER 3782; SER 6624, 8438, 8446, 8470, 12514. Based on these representations, and its later finding that Pierce's claim in Texas was "entirely consistent" with its own judgment, which was not based on a "finding of an 'agreement' between [Vickie] and [Howard] to give her one-half of all his property," the bankruptcy court ultimately permitted Pierce to proceed in the limited fashion he had represented to the bankruptcy court. *Marshall*, 273 B.R. at 826-27, 831-32; SER 8585-86, 12261 & n.2.

Vickie thereafter participated in the probate-court trial only as a counterdefendant, App. 21, 232, and none of her earlier-proposed jury questions was presented to the jury, SER 12260-61 & n.2; *compare* ER 3713-99 *with* ER 4076-77. Pierce obtained a judgment against Vickie based on his "no agreement" theory, which became final in February 2002. App. 92; *Marshall*, 273 B.R. at 826-27; SER 12260-61 & n.2. Explaining the scope of its judgment, the probate court confirmed that it "didn't try any issue of tortious interference with inter vivos gift in this case at all" and only decided "all the issues concerning the Estate"

and "[n]ot anything to do with what complaints that [Vickie] has against [Pierce]." SER 8660, 8664.[6]

C. The District Court Proceedings.

Shortly after the bankruptcy court entered judgment and over a year before the Texas probate judgment became final, Pierce appealed the bankruptcy court judgment to the district court. App. 20, 96.

The district court concluded that Vickie's counterclaim was a compulsory counterclaim to Pierce's defamation claim; however, it also held the counterclaim was not a "core" proceeding because of certain post-pleading developments, such as the amount Vickie recovered on the counterclaim and the bankruptcy court's rationale in dismissing Pierce's claim. App. 236-38, 265-83; SER 12204. It therefore treated the bankruptcy court's judgment as proposed and

[6] Notably, the gift Howard intended was an irrevocable gift during his lifetime, not a testamentary disposition. App. 136-48, 233, 316-20, 330-31; SER 11788. And Pierce conceded that Howard could have funded Vickie's gift during his lifetime by borrowing against his assets, without ever taking funds from the living trust. Pierce's Substituted Reply Br. 2, Sept. 18, 2003 (9th Cir. docket entry 98) ("the Living Trust's terms allowed J. Howard to borrow against his assets up until the day he died," so that "if he had really wanted to give Vickie a large gift, he could have notwithstanding the exchanges [of property] in the Living Trust"). Indeed, Howard's attorney contemplated funding the trust by issuing notes or stock measured by an increase in value of Howard's Koch stock. SER 9567.

undertook a "comprehensive, complete and independent review of" the issues. App. 97, 284.

Pierce subsequently moved for summary judgment, claiming res judicata and collateral estoppel based on the Texas probate judgment. The district court denied the motion on the grounds that the requisite identity of issues was lacking, that Pierce's motion was untimely and that applying preclusion in these circumstances was fundamentally unfair. App. 56 n.32, 223-33.

In March 2002, about a month after the Texas judgment had become final, the district court affirmed the bankruptcy court's findings and entered judgment for Vickie. App. 91, 194-95, 215-16. It concluded Howard had directed his lawyers to prepare an inter vivos trust for Vickie's benefit consisting of half the appreciation of his assets from the date of their marriage, App. 134-48, 198-202, but that Pierce conspired to suppress or destroy the trust instrument and to strip Howard of his assets, App. 145-202, 211-14.

It awarded compensatory damages of approximately $44.3 million and the same amount in punitive damages, finding "overwhelming" evidence of Pierce's "willfulness, maliciousness, and fraud." App. 26, 212, 214.[7] It characterized Pierce's litigation

[7] While the district court agreed with the bankruptcy court that Howard intended to give Vickie half the increase of his assets from the date of their marriage, it valued the increase only until the date of Howard's death, while the bankruptcy court valued it through the date of trial. App. 204.

tactics as "the height of bad faith," App. 148-49 n.21, noted that if the evidence of the trust for Vickie had been insufficient "the discovery abuses in this case might have led the Court to deem this fact as established," App. 137 n.17, and "encourage[d]" the Justice Department to investigate Pierce's chief witness, Edwin Hunter, for perjury prosecution, App. 160 n.28.

D. Ninth Circuit Appeal I.

Pierce appealed and Vickie cross-appealed. App. 26-27. The Ninth Circuit reversed the judgment, concluding the probate exception to federal jurisdiction barred Vickie's counterclaim. *Id.*

In May 2006, this Court unanimously reversed and remanded to the Ninth Circuit for further proceedings to consider whether Vickie's claim was core and to address claim and issue preclusion. *Marshall v. Marshall*, 547 U.S. 293, 315 (2006).[8]

E. Ninth Circuit Appeal II.

On March 19, 2010, nearly four years after remand, the Ninth Circuit again reversed the district court's judgment in favor of Vickie, holding that her compulsory counterclaim was not a core proceeding under 28 U.S.C. §157(b)(2)(C); her bankruptcy court

[8] Shortly after remand, Pierce died, and several months later, Vickie died; each was substituted on the appeal by the respective executor of the estate. App. 5-6 n.1.

judgment was therefore not "final"; and her district court judgment, entered after the Texas probate judgment, was barred by that judgment on the ground of issue preclusion. App. 55-58, 64-65.

In so concluding, the Ninth Circuit made several significant rulings:

- Vickie's counterclaim was a compulsory counterclaim to Pierce's proof of claim, "because the 'operative facts underlying [her] action' are the same as those underlying [Pierce's] defamation claim" and "[t]he defamation claim, [Vickie's] affirmative defense of truth, and her counterclaim for tortious interference all concern the alleged efforts by [Pierce] to obtain control of his father's estate" through improper means, App. 47-48 & n.29;

- Core jurisdiction can exist over a counterclaim "based upon state law, not the Bankruptcy Code or something else that is unique to the bankruptcy context," even if the counterclaim "could have been brought in state court," App. 43-44 & nn.26, 27;

- The determination whether a counterclaim to a proof of claim is core under §157(b)(2)(C) "must focus largely on what is available to the court at the time of filing, that is, the parties' pleadings," App. 51-52;

- Vickie's success on her counterclaim would defeat Pierce's defamation claim by establishing the affirmative defense of truth, App. 47-48, 55.

Although these holdings supported the conclusion that Vickie's counterclaim was core, the court – relying principally on *Katchen v. Landy*, 382 U.S. 323 (1966) and *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982) (*Marathon*) – narrowly construed §157(b)(2)(C) to mean that even a compulsory counterclaim to a proof of claim does not qualify as core unless it is "'so closely related to the proof of claim that the resolution of the counterclaim is necessary to resolve the allowance or disallowance of the claim itself.'" App. 49-50. It held Vickie's compulsory counterclaim was non-core because even if she proved through her counterclaim that the alleged defamatory statements were true, thus defeating Pierce's proof of claim, she would have had to prove additional facts to prevail on her counterclaim, including damages; therefore, "its resolution was not a necessary precursor" to resolving Pierce's defamation claim against the estate and it "was not so closely related to his claim that they essentially merged, with her counterclaim becoming part and parcel of the bankruptcy court's claims determination and allowance process." App. 4, 49-50, 55.

To hold otherwise, the court concluded, would be "an expansive reading of §157(b)(2)(C) [that] would certainly run afoul of the Court's holding in *Marathon*" and "arguably be inconsistent with the

Congress' intent to revise the Bankruptcy Code in a manner consistent with the principles of *Marathon* to make its jurisdictional grant constitutional." App. 46.

Because the conclusion that Vickie's counterclaim was non-core meant her bankruptcy judgment was not final when entered in December 2000, the Ninth Circuit, as noted above, reversed the district court judgment on the ground of issue preclusion, concluding that the Texas probate court's judgment was the earliest final judgment on "several of the legal and factual issues that Vickie Lynn Marshall sought to litigate in the bankruptcy proceeding." App. 4-5, 55-56, 58, 64. The Ninth Circuit never addressed the district court's determination that binding her to the Texas court's findings would be fundamentally unfair. App. 56 n.32, 232.

Vickie petitioned for rehearing *en banc* on the ground that the opinion erred in determining her counterclaim was non-core. App. 348-77. She also sought panel rehearing based on the panel's failure to determine whether the district court properly exercised its discretion to deny issue preclusion on fundamental fairness grounds. *Id.* The petition was denied. App. 337-38.

This Court granted certiorari on September 28, 2010.

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SUMMARY OF ARGUMENT

Purporting to follow *Marathon*, 458 U.S. 50, and *Katchen*, 382 U.S. 323, the Ninth Circuit has held that, even though 28 U.S.C. §157(b)(2)(C) empowers bankruptcy courts to finally adjudicate "counterclaims by the estate against persons filing claims against the estate," Article III forecloses them from finally adjudicating even a *compulsory* counterclaim to a claim against the estate – unless the counterclaim's resolution is a "necessary precursor" to resolving the creditor's claim and "so closely related to [the] claim that they essentially merge[], with [the] counterclaim becoming part and parcel of the bankruptcy court's claims determination and allowance process." App. 4.

Thus, even though Pierce forced Vickie to file her compulsory counterclaim in the bankruptcy by filing his proof of claim for defamation, even though success on her counterclaim would necessarily defeat his proof of claim by establishing the affirmative defense of truth, and even though the counterclaim arose out of the same transaction that Pierce placed at issue by seeking a distribution from the bankruptcy estate, the Ninth Circuit concluded that the bankruptcy court could not resolve Pierce's claim and Vickie's compulsory counterclaim together. The Ninth Circuit's new test, which effectively reverses settled bankruptcy practice both before and after *Marathon*, is insupportable.

• ***Congress intended that §157(b)(2)(C) empower bankruptcy courts to enter final judgment on all compulsory counterclaims to proofs of claim.*** The Ninth Circuit's test contravenes congressional intent. Section 157(b)(2)(C)'s plain language and the legislative history behind the 1984 Bankruptcy Act show that Congress intended to confer core jurisdiction over *all* estate counterclaims to proofs of claim and that Congress drafted the 1984 Act to conform to its understanding of *Marathon*'s constitutional strictures.

Not only does the Ninth Circuit's construction reduce §157(b)(2)(C) to surplusage – since Congress already specified in §157(b)(2)(B) that core proceedings include the "allowance or disallowance of claims against the estate" – its splintered approach to bankruptcy jurisdiction will confound bankruptcy administration and directly undermine the efficiencies Congress intended. Because Congress meant what it said in §157(b)(2)(C), the true question on appeal is whether §157(b)(2)(C)'s grant of core jurisdiction over all compulsory counterclaims is constitutional.

• ***Section 157(b)(2)(C)'s grant of core jurisdiction over all compulsory counterclaims is constitutional.*** This Court has acknowledged repeatedly that its Article III precedents "do not admit of easy synthesis." *Commodity Futures Trading Comm'n v. Schor*, 478 U.S. 833, 847 (1986) (*Schor*). Nonetheless, our brief shows that §157(b)(2)(C)'s grant of core jurisdiction over all compulsory counterclaims is

constitutional under each of this Court's various announced standards and considerations, whether viewed individually or collectively. For example:

This Court's pre- and post-*Marathon* precedent recognizes that creditors submitting proofs of claim for adjudication to non-Article III bankruptcy judges acquiesce to the adjudication of integrally-related counterclaims because they invoke the benefits of claims allowance, a process integral to the restructuring of debtor-creditor relations. A creditor seeking such distribution from the estate must also accept the burdens of the bankruptcy process, including the bankruptcy court's equitable power to issue complete relief over the entire dispute that the creditor placed at issue.

Core jurisdiction over all compulsory counterclaims is also consistent with this Court's post-*Marathon* precedent assessing the congressional delegation of decisionmaking to non-Article III tribunals by considering practical consequences of the adjudicatory scheme in light of the concerns underlying Article III. Core jurisdiction over all compulsory counterclaims tracks historical practice, promotes Congress' goals of efficient bankruptcy administration, and falls within Congress' plenary Article I power over bankruptcies. Conversely, it poses only a *de minimis* intrusion on the separation-of-powers concerns that underlie Article III and much of *Marathon*.

Finally, core jurisdiction over all compulsory counterclaims comports with this Court's post-*Marathon*

cases upholding non-Article III adjudication of "public rights," which includes private rights closely integrated with public regulatory schemes, and with this Court's precedent upholding factfinding by specialized adjuncts to Article III courts.

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ARGUMENT

I. CONGRESS INTENDED FOR 28 U.S.C. §157(b)(2)(C) TO EMPOWER BANKRUPTCY COURTS TO RENDER FINAL JUDGMENT ON ALL COMPULSORY COUNTERCLAIMS TO CREDITOR CLAIMS AGAINST THE ESTATE AND IT DRAFTED THE STATUTE TO CONFORM TO *MARATHON*'S CONSTITUTIONAL STRICTURES.

A. Backdrop To *Marathon*, The 1984 Bankruptcy Act And §157(b)(2)(C).

1. Prior to the 1978 Bankruptcy Act, bankruptcy referees exercised the summary jurisdiction in bankruptcy of the district court, including the determination of compulsory counterclaims to proofs of claim.

Before Congress enacted the 1978 Bankruptcy Act ultimately invalidated by *Marathon*, bankruptcy proceedings were either summary or plenary under the 1898 Bankruptcy Act. *Marathon*, 458 U.S. at 53. District courts sitting in bankruptcy, and referees to whom they could refer matters and who lacked Article III salary and tenure protections, had summary

jurisdiction to adjudicate controversies regarding property in the court's actual or constructive possession (such as creditor claims against the estate) and even "plenary" claims (for example, actions involving property in the possession of third parties) where the parties expressly or impliedly consented to adjudication. *Id.*; *Katchen*, 382 U.S. at 327-32 & n.9.

"The referee would initially hear and decide practically all matters arising in the proceedings, including the allowance and disallowance of the claims of creditors." *Marathon*, 458 U.S. at 99 (White, J., dissenting). The bankruptcy referees were subordinate adjuncts of the district courts; the district courts appointed and removed them and had absolute discretion to refer or withdraw the reference of the bankruptcy case. *Id.* at 79 n.31.

When a creditor filed a proof of claim in the bankruptcy, the district court and the non-Article III bankruptcy referees generally had summary jurisdiction over the bankruptcy trustee's compulsory counterclaims. 1 Alan N. Resnick & Henry J. Sommer, Collier on Bankruptcy, ¶3.02[3][d][i], p. 3-32 (16th ed. 2010); *see, e.g.*, *Peters v. Lines*, 275 F.2d 919, 924-25 (9th Cir. 1960); *In re Majestic Radio & Television Corp.*, 227 F.2d 152, 156 (7th Cir. 1955).[9]

[9] Courts were split as to whether summary jurisdiction extended to unrelated or permissive counterclaims to proofs of claim. 1 Collier on Bankruptcy, *supra*, ¶3.02[3][d][i], at 3-32; *compare Peters*, 275 F.2d at 924-25 *with Inter-State Nat'l Bank of Kansas City v Luther*, 221 F.2d 382, 389-90 (10th Cir. 1955).

In *Katchen*, this Court upheld a bankruptcy referee's summary jurisdiction to decide a trustee's counterclaim to recover a voidable preference from a creditor who filed a proof of claim, irrespective of whether the preference counterclaim arose from the same transaction as the proof of claim. 382 U.S. at 326 n.1. It held that, even though the trustee would have had to file a plenary action to recover the preference had the creditor not filed a proof of claim, the bankruptcy court could enter a money judgment for the amount of the preference counterclaim because, inter alia, (a) having "'invoke[d] the aid of the bankruptcy court by offering a proof of claim and demanding its allowance,'" the creditor "'must abide the consequences of that procedure'" and submit to the bankruptcy court's jurisdiction to decide "'all matters in dispute [between the parties] and decree complete relief'"; (b) the counterclaim was "part and parcel of the [claims] allowance process"; and (c) there was no jury trial right because issues that arise "as part of the process of allowance or disallowance of claims" are triable in equity. *Id.* at 327-28, 330-32 & n.9, 335-38.

After *Katchen*, some commentators argued that creditors who file proofs of claim should be held to acquiesce to summary jurisdiction over any debtor counterclaim. *See In re Depo*, 40 B.R. 537, 541-42 (N.D.N.Y. 1984) (citing authorities). Yet, most courts held that a proof of claim established the creditor's submission to summary jurisdiction over "same transaction" counterclaims plus permissive counterclaims

statutorily connected to claims allowance, such as preferences or voidable transfers. *See, e.g., id.*; *In re Carnell Constr. Corp.*, 424 F.2d 296, 298-99 (3d Cir. 1970); *In re L.A. Trust Deed & Mortg. Exch.*, 464 F.2d 1136, 1138-39 (9th Cir. 1972).

2. In the 1978 Bankruptcy Act, Congress expanded the jurisdiction of non-Article III bankruptcy judges to encompass all proceedings relating to bankruptcy and substantially reduced control by Article III judges.

In the Bankruptcy Act of 1978, Congress eliminated the summary/plenary distinction, substantially broadening bankruptcy jurisdiction by conferring on non-Article III bankruptcy courts jurisdiction over all "civil proceedings arising under title 11 [the Bankruptcy title] or arising in or related to cases under title 11" and by vesting them with "all of the 'powers of a court of equity, law and admiralty.'" *Marathon*, 458 U.S. at 54-55 & n.3 (emphasis omitted). In contrast to the 1898 Act, bankruptcy courts were "'independent of the United States district courts'" and the President (instead of the district courts as before) appointed the bankruptcy judges (to 14-year terms), with the advice and consent of the Senate. *Id.* at 53, 79 n.31.

B. Congress Enacted The 1984 Bankruptcy Act To Comply With *Marathon*'s Constitutional Concerns.

1. *Marathon*'s plurality and concurrence.

In its 1982 *Marathon* decision, which triggered four separate opinions, none of which commanded a majority, this Court held the 1978 Act was unconstitutional because it authorized a bankruptcy judge lacking Article III tenure and salary guarantees to determine state common law (contract and tort) claims the debtor had commenced against a non-creditor defendant (Marathon) that had not filed a proof of claim or otherwise previously appeared in the bankruptcy case. *Id.* at 76, 87 (plurality), 89-91 (Rehnquist, J., concurring), 92 (Burger, C.J., dissenting).

The plurality: The four-justice plurality concluded that the Court had previously upheld congressional grants of plenary power directly to non-Article III tribunals only in relation to territorial courts, military courts, and legislative courts and administrative agencies adjudicating "public rights." *Id.* at 63-71. It concluded that the debtor's contract claims, which merely sought damages from a non-creditor defendant to augment the estate, could not be deemed a public right, because

> the restructuring of debtor-creditor relations, which is at the core of the federal bankruptcy power, must be distinguished from the adjudication of state-created private rights, such as the right to recover contract damages that

> is at issue in this case. The former may well be a "public right," but the latter obviously is not.

Id. at 71. The plurality's constitutional concern focused on the "broad range of questions that can be brought into a bankruptcy court because they are 'related to cases under title 11.'" *Id.* at 74.

The plurality also concluded that the Act did not fall within the Court's precedent approving "the use of administrative agencies and magistrates as adjuncts to Art. III courts," because bankruptcy courts were not true adjuncts under the new act. *Id.* at 77-87. It concluded adjunct power was "at a minimum" for the debtor's state common law claims against the non-creditor defendant, noting that, in contrast, "[o]f course, bankruptcy adjudications themselves, as well as the manner in which the rights of debtors and creditors are adjusted, are matters of federal law." *Id.* at 84 n.36.[10]

[10] The plurality described when specialized factfinding tribunals are constitutional – language Congress later emphasized in defining bankruptcy court power under the 1984 Bankruptcy Act, *see* §I.C.2, *post*:

- "[I]t is clear that when Congress creates a substantive federal right, it possesses substantial discretion to prescribe the manner in which that right may be adjudicated – including the assignment to a[ ] [non-Article III] adjunct of some functions historically performed by judges," including factual determinations "by a specialized factfinding tribunal designed by Congress, without constitutional bar," *id.* at 80-81;

(Continued on following page)

The plurality never addressed whether non-Article III bankruptcy judges could determine estate counterclaims to proofs of claim. However, the three-justice dissent described *Katchen* as upholding a bankruptcy referee's power "to hear and decide a counterclaim against the creditor arising out of the same transaction" and noted that, had Marathon filed a claim against the estate, the bankruptcy court properly could have adjudicated the debtor's state-law claim as a counterclaim. 458 U.S. at 97 n.4, 99-100 (White, J., dissenting). The plurality did not disagree, but stated in a footnote that *Katchen* did not discuss Article III and that the 1978 Act fundamentally changed prior bankruptcy practice because bankruptcy referees formerly "were 'subordinate adjuncts of the district courts,'" were "appointed and removable only by the district court," and district courts had the power to withdraw cases from the referee. *Id.* at 79 n.31.

- "[W]hen Congress creates a statutory right, it clearly has the discretion, in defining that right, to create presumptions, or assign burdens of proof, or prescribe remedies; it may also provide that persons seeking to vindicate that right must do so before particularized tribunals created to perform the specialized adjudicative tasks related to that right," *id.* at 83; and
- Although such provisions "affect the exercise of judicial power," they are constitutional because they are "incidental to Congress' power to define the right that it has created." *Id.*

The two-justice concurrence: Acknowledging that the Court's Article III precedent does "not admit of easy synthesis," Justice Rehnquist's concurrence concluded that whatever the correct standard might be, bankruptcy courts were not adjuncts of the district court under the 1978 Act and no case "has gone so far as to sanction the type of adjudication as to which Marathon will be subjected against its will under the provisions of the 1978 Act" – a claim that arises entirely under state law because it is a traditional state common law claim ("the stuff of the traditional actions at common law tried by the courts at Westminster in 1789") that has no relation to the bankruptcy other than the plaintiff being the debtor. *Id.* at 90-91.

Chief Justice Burger explained in a separate opinion that Justice Rehnquist's concurrence establishes *Marathon*'s holding, that the holding prohibits non-Article III bankruptcy courts from adjudicating only "a relatively narrow category of claims," and that Congress could resolve the constitutional issue simply by routing *Marathon*-type claims – "ancillary common-law actions" that are "related only peripherally to an adjudication of bankruptcy under federal law" -- to the district court. *Id.* at 92 (Burger, C.J., dissenting).

2. The 1984 Act.

Congress enacted the 1984 Bankruptcy Act "for the specific purpose of curing the constitutional

problems of the scheme under which [*Marathon*] arose." *In re Mankin*, 823 F.2d 1296, 1306 (9th Cir. 1987); *accord, In re Arnold Print Works, Inc.*, 815 F.2d 165, 166 (1st Cir. 1987) (Breyer, J.) (1984 Act was "an effort to cure the constitutional defect").

Among the changes: (1) Congress conferred jurisdiction over "all civil proceedings arising under title 11, or arising in or related to cases under title 11" on the district courts and gave the district courts the discretion to refer those matters to bankruptcy judges and the power to withdraw referred matters at any time, 28 U.S.C. §§1334(a), (b), 157(a), (d); (2) bankruptcy courts were now units of the district courts, and bankruptcy judges serve as judicial officers of the district courts, 28 U.S.C. §§151, 152(a)(1); and (3) Article III judges appoint the bankruptcy judges (instead of the President and Senate) and control any removal for cause during their term, 28 U.S.C. §152(a), (e).

Consistent with *Marathon*'s limited holding, Congress also divided bankruptcy court jurisdiction into "core" proceedings, in which bankruptcy courts could render final orders subject to traditional appellate review by the district court, and proceedings that are only "related to a case under title 11," which are subject to district court de novo review absent the parties' consent to bankruptcy court determination. §§157(b)(1), (3), (c)(1)-(2), 158.

C. Congress Intended §157(b)(2)(C) To Authorize Bankruptcy Courts To Render Final Judgment On All Compulsory Counterclaims By The Estate Against Creditors Filing Claims Against The Estate.

1. The statute's plain language.

Section 157(b)(2) provides that "[c]ore proceedings include, but are not limited to" a number of specific types of proceedings. Thus, while Congress did not attempt to identify every proceeding within a bankruptcy court's core jurisdiction, §157(b)(2) "lists various types of proceedings *deemed by Congress* to be core proceedings." *Mankin*, 823 F.2d at 1299 (emphasis added). "Section 157(b)(2) does not set categorical limits on the jurisdiction of bankruptcy courts over core proceedings, but rather merely enumerates examples of proceedings falling within a bankruptcy court's core proceeding jurisdiction." *Id.* at 1300.

Accordingly, §157(b)(2)'s plain language establishes that Congress, by designating "counterclaims by the estate against persons filing claims against the estate" as core in §157(b)(2)(C), intended to empower bankruptcy courts to render final judgment on estate counterclaims to creditors' claims against the estate.

"The linguistic structure of §157 lends further support to this conclusion. Subsection (b)(1) equates core proceedings with those 'arising under title 11, or

arising in a case under title 11,' whereas subsection (c)(1) makes 'non-core' proceedings synonymous with 'otherwise related to' proceedings." *In re Toledo*, 170 F.3d 1340, 1349 (11th Cir. 1999); *see also In re Robino*, 243 B.R. 472, 493 (Bankr. N.D. Ala. 1999) (§157(b)(2) provides a "nonexclusive list of 'arising in' or 'arising under' proceedings"). Unlike the debtor's claim against the non-creditor defendant in *Marathon*, a debtor's counterclaim to a proof of claim "arises in" the bankruptcy case even if it involves rights created by state law, because the claims allowance process only exists in bankruptcy. *In re Bar M Petroleum Co.*, 63 B.R. 343, 346 (Bankr. W.D. Tex. 1986) ("[w]hile the facts alleged by the Trustee could have been the basis for a State Court suit commenced totally independently of the Chapter 11 case, the counterclaim, supported coincidentally by those same facts, could only be asserted in the Debtor's reorganization case in which the claim of Defendant was filed").[11]

[11] *See also In re Asousa P'ship*, 276 B.R. 55, 77 (Bankr. E.D. Pa. 2002) ("objections to claims [against the estate] and counterclaims which are part and parcel of the claims allowance process, by their nature, could arise only in the context of a bankruptcy case since absent the bankruptcy case, the claims allowance process would not exist"); *Robino*, 243 B.R. at 493 ("arising in" proceedings include "the filing of proofs of claims" and "counterclaims by the bankruptcy estate against filed claims" because such proceedings "would not exist outside of bankruptcy"); *In re Manville Forest Prods. Corp.*, 896 F.2d 1384, 1390 (2d Cir. 1990) (although state-law rights underlying proofs of claim are enforceable in state court absent a bankruptcy, " 'the

(Continued on following page)

A compulsory counterclaim, in particular, necessarily "arises in" the bankruptcy case because the debtor *must* file it in the bankruptcy case; if the debtor fails to assert it and the creditor's claim is successful, res judicata bars its subsequent assertion. 10 Alan N. Resnick & Henry J. Sommer, Collier on Bankruptcy, ¶7013.02, p. 7013-2 (15th ed. 2010); *Baker v. Gold Seal Liquors, Inc.*, 417 U.S. 467, 469 n.1 (1974) ("[a] counterclaim which is compulsory but is not brought is thereafter barred").

2. Legislative history.

The legislative history confirms that Congress meant what §157(b)(2)(C)'s plain language says.

Congress intended for the 1984 Act to codify judiciary-created emergency bankruptcy rules enacted in *Marathon*'s wake. 1 Collier on Bankruptcy, *supra*, ¶3.10[2][b], at 3-99; *see* 130 Cong. Rec. 6045, 6241-44 (1984) (statements of co-sponsor Reps. Kastenmeier and Kindness). Those rules prohibited bankruptcy courts from entering final judgments in "related proceedings," which included "claims brought by the estate against parties *who have not filed claims against the estate*" and did "*not* include . . . counterclaims by the estate in whatever amount

nature of the state proceeding would be different from the nature of the proceeding following the filing of a proof of claim' "; a claim against the estate is a core proceeding because " 'it could arise only in the context of bankruptcy' ").

against persons filing claims against the estate." 1 Collier on Bankruptcy, *supra*, ¶3.10[2][b], at 3-96, 3-97 n.15 (emphasis added). Congress codified that same principle – such counterclaims are not "related proceedings" – by defining them as core in §157(b)(2)(C).[12]

The legislative history demonstrates that Congress believed its mandate was constitutional. As the 1984 Act's co-sponsors explained,

> *Marathon* held only that: First, bankruptcy courts were not true adjuncts of the district courts because the district courts had no control over them; and second, a separate nonarticle III court could not properly decide State law claims that were not *integral to the core bankruptcy function of restructuring debtor-creditor rights*.

130 Cong. Rec. 6046 (co-sponsor Rep. Kastenmeier) (emphasis added); *see also id.* at 6242 (co-sponsor Rep. Kindness: "*Marathon* was concerned with a very limited kind of proceeding. . . . It was not concerned even with all bankruptcy proceedings involving

[12] The legislative history confirms Congress' intent that bankruptcy courts could render final judgment in *all* core proceedings. *See, e.g.*, 130 Cong. Rec. 6045 (Rep. Kastenmeier: the bill "authorizes bankruptcy judges to decide all core bankruptcy proceedings"); *id.* at 6242 (Rep. Kindness: "Bankruptcy judges will be able to enter a final judgment in much the same way as an article 3 judge would in all proceedings integral to the core bankruptcy functioning of restructuring the obligations of the debtor and his creditors").

questions of State law in some way. It was concerned only with State law issues that did not arise in the core bankruptcy function *of adjusting debtor-creditor rights*.") (emphasis added).

The co-sponsors emphasized the *Marathon* plurality's statements that (a) Congress has broad power when it creates statutory rights; and (b) bankruptcy adjudications and the adjustment of debtor-creditor rights are matters of federal law. *See id.* at 6046-47 (quoting *Marathon*, 458 U.S. at 83, 84 n.36); *see also* §I.B.1 & n.10, *ante*. The co-sponsors explained that in contrast to the claims at issue in *Marathon*, which arose entirely under state law, core bankruptcy proceedings "arise under Federal law" even where they "involve incidental questions of State law" because the proceedings are "integral to the restructuring of debtor-creditor rights." 130 Cong. Rec. 6046; *see also id.* (Rep. Kastenmeier stating that "[t]he Supreme Court previously held in *Katchen* . . . that State common law actions become transformed into Federal bankruptcy matters when brought in proceedings integral to a bankruptcy case"), *id.* at 6047 ("[s]tate law issues that arise in the course of restructuring debtor-creditor rights may be decided by a bankruptcy judge" because "[t]hese are core bankruptcy proceedings").

> In this respect, State law rights arising in core bankruptcy proceedings are functionally equivalent to congressionally created rights, because Congress has the power to modify State law rights in bankruptcy

> proceedings. . . . Indeed, the very purpose of bankruptcy is to modify the rights of the debtors and creditors, and the bankruptcy code authorizes the bankruptcy court to abrogate or modify State-created obligations in many ways.

Id. at 6047 (Rep. Kastenmeier); *see also id.* at 6243 (Rep. Kindness: *Marathon* "dealt only with noncore bankruptcy proceedings that arise under State law, outside of the bankruptcy estate, outside of but related to the bankruptcy estate").

Congress believed that *almost all proceedings* before bankruptcy judges – the co-sponsors said 95% – would be core. *Arnold Print Works*, 815 F.2d at 168-69 (Breyer, J.); *see* 130 Cong. Rec. 6045, 6047, 6240, 6242-43 (95% core); *see also id.* at 6241 (Rep. Kastenmeier: *Marathon* "held that only a narrow class of matters taken up in some bankruptcy cases could not be decided by an article I judge").[13]

The legislative history thus demonstrates that Congress, based on its reading of *Marathon*, understood that core jurisdiction constitutionally exists over all counterclaims to proofs of claim because –

[13] Representative Kastenmeier also explained that core bankruptcy jurisdiction "is broader than the summary jurisdiction of the bankruptcy courts under pre-1978 law" because "[c]ore proceedings include all those in which the right to relief is created by Federal law, whether or not the proceeding concerns property in the possession or constructive possession of the trustee." 130 Cong. Rec. 6045.

in contrast to the claim against the non-creditor third party in *Marathon* – such counterclaims are part of the core bankruptcy function of restructuring and adjusting debtor-creditor rights and they therefore arise under federal law even where the underlying claims involve rights created by state law.

D. The Ninth Circuit Approach Nullifies Congress' Intent.

1. The opinion below ignores §157(b)(2)(C)'s plain language and legislative history.

The opinion makes no legitimate attempt to reconcile its narrow construction of §157(b)(2)(C) with the statute's plain language and legislative history. Instead, it simply states that an expansive reading would "arguably be inconsistent with the Congress' intent to revise the Bankruptcy Code in a manner consistent with the principles of *Marathon* to make its jurisdictional grant constitutional." App. 46; *see also* App. 50 (stating its narrow construction comports with "Congress' desire to revise the Bankruptcy Code in a manner consistent with the Constitution").

But as this Court recognized in *Schor*, 478 U.S. 833, rejecting a circuit court's similar effort to straightjacket a counterclaim statute under *Marathon*, the canon that courts should construe statutes to avoid constitutional questions "does not give a court the prerogative to ignore the legislative will in order to avoid constitutional adjudication." 478 U.S. at 841;

see also Mankin, 823 F.2d at 1301 & n.3 (Ninth Circuit noting that although the canon that constitutional problems are to be avoided in construing statutes is apt in construing §157(b)(2)'s two catch-all provisions, subsections (A) and (O), the more apt principle in construing subsections (B)-(N) is "that the will of the legislature underlying the provision is not to be ignored").

The legislative history confirms that Congress believed that §157(b)(2)(C), as written, is constitutional under *Marathon*. By re-formulating the statute to comport with its own view of constitutionality, the Ninth Circuit impermissibly bypassed and directly contravened congressional intent.

2. The opinion below reduces §157(b)(2)(C) to surplusage.

The opinion violates cardinal rules of statutory construction in re-writing §157(b)(2)(C). Citing this Court's precedent, the opinion acknowledges that courts should avoid construing statutes "'in a manner that is strained and, at the same time, would render a statutory term superfluous.'" App. 43-44 (citing *United Sav. Ass'n of Tex. v. Timbers of Inwood Forest Assocs., Ltd.*, 484 U.S. 365, 370-71 (1988) and *Dole Food Co. v. Patrickson*, 538 U.S. 468, 477 (2003)). It applies that rule to reject Pierce's contention that Vickie's counterclaim is non-core because it could have been brought in state court and is not bankruptcy-specific, reasoning "[w]e do not believe that

Congress intended §157(b)(2)(C) to be a meaningless (or near meaningless) provision, which is what it would become under Pierce Marshall's overly restrictive approach." App. 43-44.

But the opinion, perversely, then adopts a core-jurisdiction test that renders §157(b)(2)(C) meaningless. By prohibiting core jurisdiction over a compulsory counterclaim unless it is necessary to determine the allowance or disallowance of the creditor claim and raises no issues outside that claim, the opinion makes §157(b)(2)(C) superfluous, because Congress already specified in §157(b)(2)(B) that core proceedings include the "allowance or disallowance of claims against the estate."

If Congress had intended to limit core counterclaim jurisdiction to the mere allowance/disallowance of creditor claims, as the opinion holds, it would not have included a separate counterclaim provision.

3. The opinion below flouts the congressional goals of efficient and expeditious bankruptcies.

Congress enacted the 1984 Act "to reduce substantially the time-consuming and expensive litigation regarding a bankruptcy court's jurisdiction over a particular proceeding" and to ensure "the efficient and expeditious resolution of all matters connected to the bankruptcy estate." *In re Fietz*, 852 F.2d 455, 457 (9th Cir. 1988).

It "'realized that the bankruptcy court's jurisdictional reach was essential to the efficient administration of bankruptcy proceedings and intended that the 'core' jurisdiction would be construed as broadly as possible subject to the constitutional limits established in *Marathon*.'" *In re CBI Holding Co.*, 529 F.3d 432, 459-60 (2d Cir. 2008). "By specifically including as core proceedings counterclaims brought by a debtor as a result of claims filed by creditors against the estate, Congress apparently believed that it is more efficient having a single court decide all cases based on the same facts and circumstances." *In re Fang Operators*, 158 B.R. 643, 647 (Bankr. N.D. Tex. 1993).

The Ninth Circuit's construction of §157(b)(2)(C) scuttles these goals. If upheld, it would:

- render most counterclaims non-core, because compulsory counterclaims (and permissive counterclaims even more so) will rarely "essentially merge" with the creditor's claim in terms of proof, as the Ninth Circuit's test requires;
- splinter the determination of creditor claims against the estate and compulsory counterclaims into different forums;
- produce the absurd result that debtors must file compulsory counterclaims in bankruptcy courts that cannot finally adjudicate them;

- swamp bankruptcy and district courts with abstention and withdrawal motions; and
- spawn endless litigation and confusion over jurisdictional limits and claim and issue preclusion, because district courts would end up determining counterclaims that are legally and factually interconnected to creditor claims adjudged by the bankruptcy court.

This mayhem is not what Congress intended.

* * *

In sum, §157(b)(2)(C)'s plain language and legislative history demonstrate that Congress intended to confer on bankruptcy courts core jurisdiction over all estate counterclaims against persons filing claims against the estate. While the legislative grant includes permissive counterclaims, the only constitutional question before this Court – based on the Ninth Circuit's holding and the specific questions on which certiorari was granted – is the constitutionality of bankruptcy courts hearing and deciding all *compulsory* counterclaims.[14] We now demonstrate that

[14] We also are mindful of Justice Rehnquist's warning in *Marathon*: "Particularly in an area of constitutional law such as that of 'Art. III Courts,' with its frequently arcane distinctions and confusing precedents, rigorous adherence to the principle that this Court should decide no more of a constitutional question than is absolutely necessary accords with both our decided cases and with sound judicial policy." *Marathon*, 458 U.S. at 90 (Rehnquist, J., concurring).

Congress was correct that its grant of core jurisdiction over compulsory counterclaims to proofs of claim is constitutional.

II. SECTION 157(b)(2)(C)'S GRANT OF CORE JURISDICTION OVER ALL COMPULSORY COUNTERCLAIMS IS CONSTITUTIONAL.

Article III, section 1, is facially absolute: "The judicial Power of the United States, shall be vested in one Supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish" and those judges shall "hold their offices during good Behaviour" and receive compensation that "shall not be diminished. . . ." U.S. Const. art. III, § 1. Article I is equally unlimited on its face in defining responsibility and power reserved exclusively to Congress, including the power to establish "uniform Laws on the subject of Bankruptcies throughout the United States." U.S. Const. art. I, § 8.

This Court "has long recognized that Congress is not barred from acting pursuant to its powers under Article I to vest decisionmaking authority in tribunals that lack the attributes of Article III courts." *Thomas v. Union Carbide Agr. Prods. Co.*, 473 U.S. 568, 583 (1985). Thus, there is a long history of decisionmaking by judges lacking Article III's tenure and compensation guarantees, including in territorial courts, military courts, legislative courts, agency commissions, and bankruptcy proceedings.

"The cases dealing with the authority of Congress to create courts other than by use of its power under Art. III do not admit of easy synthesis." *Marathon*, 458 U.S. at 91 (Rehnquist, J., concurring). *Marathon* did not definitively resolve the line-drawing conundrum as to when non-Article III judges are constitutionally permissible. *See id.* (concurrence declining to assess whether precedent supports "a general proposition and three tidy exceptions, as the plurality believes"); *id.* at 104 (White, J., dissenting) (describing the plurality's attempt to "cabin the domain of Art. I courts" into three narrow exceptions as "quite unrealistic" and belied by its adjunct-court discussion).

Nor has this Court's post-*Marathon* precedent clarified the uncertainty. *See, e.g.*, *Schor*, 478 U.S. at 847 ("our precedents in this area do not admit of easy synthesis"); *Thomas*, 473 U.S. at 583 ("[a]n absolute construction of Article III is not possible in this area of 'frequently arcane distinctions and confusing precedents'").

Given the absence of a precedential synthesis, we show below that §157(b)(2)(C)'s grant of core jurisdiction over all compulsory counterclaims is constitutional under this Court's various announced theories and considerations, whether viewed individually or collectively.

A. Creditors Who Submit Claims Against The Estate To The Non-Article III Bankruptcy Court Invoke That Court's Equitable Jurisdiction To Resolve All Compulsory Counterclaims.

1. *Marathon* did not alter the basic principle that the filing of a proof of claim invokes the special rules of bankruptcy.

Although some lower courts at first construed *Marathon* as broadly invalidating non-Article III adjudications, this Court quickly clarified that *Marathon*'s constitutional strictures are narrow and that the *Marathon* concurrence -- whose conclusion solely turned on the fact that the case involved a debtor's common law claims against a non-creditor defendant that were only peripherally related to the bankruptcy case – established the holding. *See Thomas*, 473 U.S. at 584 (noting the "divided [*Marathon*] Court was unable to agree on the precise scope and nature of Article III's limitations" and the holding "establishes only that Congress may not vest in a non-Article III court the power to adjudicate, render final judgment, and issue binding orders in a traditional contract action arising under state law, without consent of the litigants, and subject only to ordinary appellate review"); *Schor*, 478 U.S. at 838-39, 847-48 (same).

In so doing, the Court effectively confirmed that Congress was correct in narrowly construing *Marathon*'s constitutional strictures when enacting the 1984 Act. *See In re Kaiser Steel Corp.*, 95 B.R. 782,

787 (Bankr. D. Colo. 1989) ("The holdings of *Schor* and *Thomas* in the bankruptcy setting had, in fact, been anticipated by Congress in the enactment of 28 U.S.C. §157(c)(2)").

The crucial distinction is that *Marathon* did not involve a debtor's counterclaim to a proof of claim. As the Second Circuit recently summarized, *Marathon* merely held that "a non-Article III bankruptcy judge could not adjudicate a pre-petition contract dispute arising under state law against a party that had not filed a proof of claim and was not otherwise related to the bankruptcy proceedings," and *Marathon* distinguished that type of dispute from " 'the restructuring of debtor-creditor relations, which is at the core of the federal bankruptcy power.' " *CBI*, 529 F.3d at 459-60 (emphasis added); *see also In re SG Philips Constructors, Inc.*, 45 F.3d 702, 706 (2d Cir. 1995) (the *Marathon* defendant was "involuntarily subjected to having the debtor's state law claim against it decided by an Article I judge" because it "had not filed a proof of claim and had no other connection with the bankruptcy").

Nothing in *Marathon* " 'alters the basic principle that the filing of a proof of claim invokes the special rules of bankruptcy. . . .' " *CBI*, 529 F.3d at 462; *see id.* at 437-38, 442, 459-65 (upholding core jurisdiction over $70 million tort and contract counterclaims filed against $210,000 proof of claim for unpaid services).

2. This Court's post-*Marathon* decisions confirm the constitutionality of non-Article III bankruptcy judges resolving all compulsory counterclaims to proofs of claim.

a. *Granfinanciera* and *Langenkamp*.

In *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33 (1989), this Court held that Congress could not deprive defendants who had not filed proofs of claim of their jury-trial right on a trustee's fraudulent conveyance action, reasoning that the "fraudulent conveyance action does not arise 'as part of the process of allowance or disallowance of claims'" and is not "integral to the restructuring of debtor-creditor relations." *Id.* at 58; *see also id.* at 60 (fraudulent conveyance actions are "not integrally related to the reformation of debtor-creditor relations").

The Court cited *Katchen* as "mak[ing] clear" that "by submitting a claim against the bankruptcy estate, creditors subject themselves to the [bankruptcy] court's equitable power to disallow those claims, even though the debtor's opposing counterclaims are legal in nature and the Seventh Amendment would have entitled creditors to a jury trial had they not tendered claims against the estate." *Id.* at 59 n.14. Thus, while non-Article III bankruptcy courts can resolve debtors' preference or fraudulent conveyance claims when they arise as counterclaims to proofs of claim, a jury-trial right exists if the defendant never filed a proof of claim. *See id.* at 56-59, comparing *Schoenthal v.*

Irving Trust Co., 287 U.S. 92 (1932) (no proof of claim) to *Katchen*, 382 U.S. 323 (proof of claim filed).

The *Granfinanciera* court analogized the fraudulent conveyance action to the debtor's claims against the non-creditor defendant in *Marathon*, in that it did not involve creditors' "claims to a pro rata share of the bankruptcy res" and "more nearly resemble[d] state-law contract claims brought by a bankrupt corporation to augment the bankruptcy estate." *Granfinanciera*, 492 U.S. at 56. Because the defendants in the fraudulent conveyance action had not filed a claim against the estate, the Seventh Amendment entitled them to a jury trial notwithstanding Congress' designation of fraudulent conveyance actions as "core proceedings." *Id.* at 36.

Langenkamp v. Culp, 498 U.S. 42 (1991), decided two years later, determined the flip side of *Granfinanciera* – the defendants there did file proofs of claim, so the trustee's avoidable preference claims were filed as counterclaims to creditors' claims against the estate. 498 U.S. at 42-43. Accordingly, the Court held the creditors were not entitled to a jury trial on the counterclaims because "by filing a claim against a bankruptcy estate the creditor triggers the process of 'allowance and disallowance of claims,' thereby subjecting himself to the bankruptcy court's equitable power," and the trustee's preference counterclaim "becomes part of the claims-allowance process which is triable only in equity." 498 U.S. at

44.[15] Thus, "the creditor's claim and the ensuing preference action by the trustee become integral to the restructuring of the debtor-creditor relationship through the bankruptcy court's equity jurisdiction." *Id.* (emphasis omitted).

Although *Granfinanciera* and *Langenkamp* involved the right to jury trial, *Granfinanciera* holds that the question of whether the Seventh Amendment permits Congress to assign the adjudication of a statutory cause of action that is legal in nature "to a tribunal that does not employ juries as factfinders requires the same answer as the question whether Article III allows Congress to assign adjudication of that cause of action to a non-Article III tribunal." *Granfinanciera*, 492 U.S. at 53.

[15] The principle that bankruptcy courts are specialized courts of equity with respect to claims allowance is well rooted in this Court's jurisprudence. *See, e.g., Barton v. Barbour*, 104 U.S. 126, 134 (1881) ("[I]n cases of bankruptcy, many incidental questions arise in the course of administering the bankrupt estate, which would ordinarily be pure cases at law, and in respect of their facts triable by jury, but, as belonging to the bankruptcy proceedings, they become cases over which the bankruptcy court, which acts as a court of equity, exercises exclusive control Thus, a claim of debt of damages against the bankrupt is investigated by chancery methods."); *Pepper v Litton*, 308 U.S. 295, 307 (1939) ("the bankruptcy court in passing on allowance of claims sits as a court of equity"); *Atlas Roofing Co. v. Occupational Safety & Health Review Comm'n*, 430 U.S. 442, 454 n.11 (1977) (as recognized in *Curtis v. Loether*, 415 U S. 189, 194-95 (1974) and *Katchen*, "a bankruptcy court, exercising its summary jurisdiction, was a specialized court of equity").

Thus, although Justice Brennan noted in the *Marathon* plurality that *Katchen* did not discuss "the Art. III issue" (*Marathon*, 458 U.S. at 79 n.31, plurality opinion), he later explained in *Granfinanciera* that bankruptcy jury-trial decisions such as *Katchen*, *Granfinanciera* and *Langenkamp* are germane to the Article III issue. *See also Curtis*, 415 U.S. at 195 (citing *Katchen* as upholding "congressional power to entrust enforcement of statutory rights to an administrative process or specialized court of equity free from the strictures of the Seventh Amendment").

Katchen, *Granfinanciera* and *Langenkamp* all support the constitutionality of non-Article III bankruptcy judges resolving all compulsory counterclaims to proofs of claim. Compulsory counterclaims to proofs of claim necessarily arise "as part of the process of allowance or disallowance of claims" and are "integral to the restructuring of the debtor-creditor relations," the same as the preference and fraudulent conveyance counterclaims at issue in *Katchen* and *Langenkamp*. *See In re Yagow*, 53 B.R. 737, 740 (Bankr. D.N.D. 1985) ("[a] counterclaim, compulsory in nature, is the type of counterclaim which would be considered integral"); *In re Beugen*, 81 B.R. 994, 1000 (Bankr. N.D. Cal. 1988) ("[a] compulsory counterclaim against a creditor that has asserted a claim is closely connected to the central bankruptcy function of determining claims"); *Asousa P'ship*, 276 B.R. at 66 ("counterclaims that could affect the allowance or disallowance of a proof of claim are part and parcel of the claims allowance process").

By definition, compulsory counterclaims arise out of the same transaction that the creditor, by filing the proof of claim, submitted to the bankruptcy court for resolution and constitute potential affirmative defenses to the creditor's claim. Here, for example, success on Vickie's counterclaim for tortious interference with gift would necessarily defeat Pierce's proof of claim by establishing the affirmative defense of truth to the defamation allegations. App. 47-48, 55. Moreover, compulsory counterclaims – since they arise from the same transaction as the claim that triggered their filing – fall within a court's ancillary jurisdiction and need no independent jurisdictional basis. *Baker v. Gold Seal Liquors, Inc.*, 417 U.S. at 469 n.1. Proofs of claim and the bankruptcy estate's resulting compulsory counterclaims are two halves of a single dispute.

b. *Schor.*

In *Schor*, this Court effectively recognized that *Katchen*'s analysis of preference counterclaims extends to all compulsory counterclaims. In upholding the constitutionality of Congress authorizing non-Article III commissioners of the Commodity Futures Trading Commission to adjudicate counterclaims "'aris[ing] out of the transaction or occurrence or series of transactions or occurrences set forth in the complaint,'" the Court observed that such jurisdiction was "not without precedent" because *Katchen* upholds "a bankruptcy referee's power to hear and decide state law counterclaims against a creditor who filed a

claim in bankruptcy when those counterclaims arose out of the same transaction." *Schor*, 478 U.S. at 833, 852; *see also Marathon*, 458 U.S. at 97 n.4 (White, J., dissenting) (*Katchen* recognizes "that when a creditor files a claim, the [bankruptcy] referee is empowered to hear and decide a counterclaim against that creditor arising out of the same transaction").

3. In addition, longstanding precedent holds that creditors, by submitting claims against the estate to a non-Article III bankruptcy court for adjudication, invoke that court's equitable power to resolve the entire dispute and issue complete relief.

Core jurisdiction over all compulsory counterclaims is equally compelled by the fact that bankruptcy courts "passing on allowance of claims" sit as courts of equity and therefore apply "principles and rules of equity jurisprudence." *Pepper v. Litton*, 308 U.S. at 305-07; *accord*, *Katchen*, 382 U.S. at 334-38; *see also Young v. United States*, 535 U.S. 43, 50 (2002) (bankruptcy courts "are courts of equity and 'appl[y] the principles and rules of equity jurisprudence'").

A fundamental principle of equity jurisprudence, as recognized and followed in *Katchen*, is that courts of equity "'having jurisdiction of the parties to controversies brought before them, they will decide all matters in dispute and decree complete relief.'" *Katchen*, 382 U.S. at 335 (quoting *Alexander v. Hillman*, 296 U.S. 222, 241-42 (1935)). *Katchen* held that

the rationale of *Alexander v. Hillman*, a receivership case, was "equally applicable" to the bankruptcy referee's power to hear and decide the trustee's preference counterclaim. *Katchen*, 382 U.S. at 335-36; *see Granfinanciera*, 492 U.S. at 59 n.14 (noting *Katchen* "adopted a rationale articulated in *Alexander v. Hillman*").

Hillman involved an equity receivership created for the purposes of liquidating a corporation and distributing its assets. 296 U.S. at 230. After officers of the corporation filed claims to share in distribution of the receivership res, the receiver counterclaimed for affirmative relief, alleging the claimant-officers fraudulently diverted corporate funds for their own benefit and received excessive salaries. *Id.* at 235-36. The officers argued they were entitled to plenary determination of the counterclaims in the state of their residence. *Id.* at 236, 238.

This Court held that the officers, by filing claims to participate in the receivership res, "subjected themselves to all the consequences that attach to an appearance." *Id.* at 241. The receivership court therefore could adjudicate the counterclaims to "decide all matters in dispute and decree complete relief," even though the counterclaims exceeded the officers' claims against the receivership res. *Id.* at 242-43. This Court rejected the argument that the receiver must split the causes of action by adjudicating the counterclaims only to the extent they are "purely defensive" and "go to another court to recover the rest." *Id.*

In *Katchen*, this Court recognized that the *Hillman* rationale equally applied to summary proceedings before bankruptcy referees, and that bankruptcy referees are empowered to issue affirmative relief on preference counterclaims, even if the amount exceeds the proof of claim. *See Granfinaciera*, 492 U.S. at 59 n.14 (noting *Katchen* stands for the proposition that, once a creditor files a claim against the bankruptcy estate, the trustee may recover the full amount of any preference, "even if that amount exceeds the amount of the creditor's claim").

Katchen recognized that, just as the *Hillman* claimants could not invoke the receivership court's equity jurisdiction by filing claims against the res but then preclude that court from resolving the entire dispute, so too a creditor cannot invoke the aid of the bankruptcy referee by filing a claim against the bankruptcy estate but then deny that court the ability to decide the entire dispute and issue complete relief. *Katchen*, 382 U.S. at 335-36.

This rationale applies equally to all compulsory counterclaims to proofs of claim.[16] In stark contrast to

[16] Circuit courts, construing the 1898 Bankruptcy Act, recognized that *Hillman*'s rationale supported summary jurisdiction over compulsory counterclaims to proofs of claim. *See, e.g., Florance v. Kresge*, 93 F.2d 784, 786 (4th Cir. 1938); *Floro Realty & Inv. Co. v. Steem Elec. Corp.*, 128 F.2d 338, 340-41 (8th Cir. 1942); *In re Solar Mfg. Corp.*, 200 F.2d 327, 329-31 (3d Cir. 1952); *Conway v. Union Bank of Switz.*, 204 F.2d 603, 607 (2d Cir. 1953); *Cont'l Cas. Co. v. White*, 269 F.2d 213, 214-15 (4th Cir. 1959); *Inter-State Nat'l Bank of Kansas City v. Luther*, 221

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the non-creditor in *Marathon* whom the debtor involuntarily dragged into the bankruptcy, a creditor cannot ask the bankruptcy court to determine its right to distribution from the bankruptcy estate, while denying that court the ability to resolve the entire dispute and issue complete relief. By invoking the aid of the bankruptcy court, the creditor "risk[s] all of the disadvantages which may flow to him as a consequence, as well as gaining all of the benefits." *Case v. L.A. Lumber Prods. Co.*, 308 U.S. 106, 126-27 (1939). "A debtor as well as a creditor who invokes the aid of the federal courts in reorganization or rehabilitation . . . assumes all of the consequences which flow from that jurisdiction. Once the property is in the hands of the court private rights as respect that res are subject to the superior dominion of the court and are to be adjudicated pursuant to the standards prescribed by the Congress." *Id.* at 125.[17]

F.2d at 388-89; *In re Carnell Constr. Corp.*, 424 F.2d at 298-99; *In re L.A. Land & Invs. Ltd.*, 447 F.2d 1366, 1367 (9th Cir. 1971)

[17] *See also Wiswall v. Campbell*, 93 U.S. 347, 351 (1876) ("Every person submitting himself to the jurisdiction of the bankrupt [sic] court in the progress of the cause, for the purpose of having his rights in the estate determined, makes himself a party to the suit, and is bound by what is judicially determined in the legitimate course of the proceeding. A creditor who offers proof of his claim, and demands its allowance, subjects himself to the dominion of the court, and must abide the consequences.").

B. Core Jurisdiction Over All Compulsory Counterclaims To Proofs Of Claim Is Constitutional Under The *Thomas/Schor* "Purposes Of Article III" Approach.

In *Thomas*, after noting the justices could not agree on Article III's scope in *Marathon*, this Court mandated that "practical attention to substance rather than doctrinaire reliance on formal categories should inform application of Article III" and that courts must consider the "concerns guiding the selection by Congress of a particular method for resolving disputes" when "assessing the degree of judicial involvement required by Article III." 473 U.S. at 569, 587.

The next year, in *Schor*, the Court similarly rejected "formalistic and unbending rules" that might "unduly constrict Congress' ability to take needed and innovative action pursuant to its Article I powers." 478 U.S. at 851; *see also id.* at 857 ("bright-line rules cannot effectively be employed"). It held that "the constitutionality of a given congressional delegation of adjudicative functions to a non-Article III body must be assessed by reference to the purposes underlying the requirements of Article III" and therefore "due regard must be given in each case to the unique aspects of the congressional plan at issue and its practical consequences in light of the larger concerns that underlie Article III." *Schor*, 478 U.S. at 847, 857.

Core jurisdiction over all compulsory counterclaims is constitutional under the *Thomas/Schor* approach of focusing on the purposes of Article III.

1. Core jurisdiction over all compulsory counterclaims is fair to creditors who seek to share in the bankruptcy estate.

Article III, section 1's "guarantee of an independent and impartial adjudication by the federal judiciary of matters within the judicial power of the United States . . . serves to protect primarily personal, rather than structural, interests." *Schor*, 478 U.S. at 848. It "does not confer on litigants an absolute right to the plenary consideration of every nature of claim by an Article III court." *Id.*

Although proofs of claim can only be filed in the bankruptcy case, creditors do not have to file proofs of claim at all. If concerned about defending compulsory counterclaims in the bankruptcy court, creditors can opt not to seek recovery from the bankruptcy estate. "[M]any creditors do not file claims" and the fact that a creditor might find unattractive the choice between submitting to the bankruptcy court's jurisdiction and foregoing a claim against the estate to avoid that jurisdiction "does not convert the choice into an

involuntary decision." *In re Lazar*, 200 B.R. 358, 380 (Bankr. C.D. Cal. 1996).[18]

A creditor's decision to file a proof of claim triggers the "traditional bankruptcy law that he who invokes the aid of the bankruptcy court by offering a proof of claim and demanding its allowance must abide the consequences of that procedure." *Gardner v. New Jersey*, 329 U.S. 565, 573 (1947) (by choosing to file proof of claim, government waived sovereign immunity as to claim's adjudication). Creditors cannot invoke the aid of the bankruptcy court, seeking the benefits of the bankruptcy process, and at the same time prevent that court from resolving the entire dispute that the proof of claim placed at issue. *See* §II.A.3, *ante*.[19] As courts construing the 1898

[18] *See, e.g., In re Applied Thermal Sys., Inc.*, 294 B.R. 784, 791 (Bankr. N.D. Okla. 2003) ("if [the creditor] was concerned about defending counterclaims in bankruptcy court, it should have foregone filing its proof of claim against the estate of [the debtor]"); *In re Lion Country Safari, Inc. Cal.*, 124 B.R. 566, 572 (Bankr. C.D. Cal. 1991) ("The filing of a proof of claim by a creditor is 'voluntary' in the sense that a creditor is not required to file a proof of claim, and pursue it within the bankruptcy court"); *In re Wiener Pharms., Inc.*, No. 086-60909-21, 1988 Bankr. LEXIS 1097, at *16 (Bankr. E.D.N.Y. June 20, 1988) ("To call it jurisdiction by ambush is simply to use pejorative terms for what is the well known consequence of filing a claim. The defendants here could have avoided the jurisdiction of the bankruptcy court by refraining from asserting a right to share in the distribution of the debtor's estate.").

[19] This Court has similarly recognized in non-bankruptcy contexts that a plaintiff, who "by his voluntary act in demanding justice from the defendant, submitted himself to the jurisdiction

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Bankruptcy Act stated in upholding summary jurisdiction over compulsory counterclaims to proofs of claim:

> No party can invite summary adjudication on only part of the relevant evidence relating to the subject matter of the claim. . . . [I]f you invite a Bankruptcy Court to review a set of facts for your benefit, you invite it to review all pertinent related facts even though they tend to prove your opponent's case.

Majestic Radio & Television Corp., 227 F.2d at 156; *accord*, *Peters v. Lines*, 275 F.2d at 924-25 ("[i]n submitting one side of a controversy for resolution logic dictates that the entire controversy should be open for resolution").[20] Nor can creditors, given

of the court, there is nothing arbitrary or unreasonable in treating him as being there for all purposes," including counterclaims. *Adam v. Saenger*, 303 U.S. 59, 67-68 (1938); *accord*, *Frank L. Young Co. v. McNeal-Edwards Co.*, 283 U.S. 398, 400 (1931) (where the plaintiff is already in court by "'his own voluntary act, it is reasonable to treat him as being there for all the purposes for which justice requires his presence'"); *Gen Elec. Co. v. Marvel Rare Metals Co.*, 287 U.S. 430, 435 (1932) ("[t]he setting up of a counterclaim against one already in a court of his own choosing is very different, in respect to venue, from hailing him into that court").

[20] Pre- and post-*Marathon*, lower courts often describe this principle as meaning creditors "impliedly consent" to compulsory-counterclaim adjudication. *See, e.g.*, *Applied Thermal Sys.*, 294 B.R. at 788-89 & n.15; *Asousa P'ship*, 276 B.R. at 66-67; *Beugen*, 81 B.R. at 1001; *In re STN Enters.*, 73 B.R. 470, 483 (Bankr. D. Vt. 1987); *In re Sun West Distribs.*, 69 B.R. 861, 864-65 (Bankr. S.D. Cal. 1987). But it is more a matter of creditors being bound

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§157(b)(2)(C)'s express language, legitimately claim surprise that their proof of claim triggered core jurisdiction over all compulsory counterclaims – claims the debtor must file to avoid relinquishing forever.[21]

Pierce, for example, admitted in his bankruptcy-court filings that "[a] review of [Vickie's] counterclaim demonstrates that the defamatory statements and the challenged transactions at issue in [Pierce's] Defamation Action are at the heart of [Vickie's] causes of action against [Pierce]. . . ." JA 107; *see also* App. 275 (district court emphasizing Pierce's statement that the defamation claim and Vickie's counterclaim were "both halves" of the same action). Pierce cannot cry foul over the bankruptcy court

by the benefits and burdens of the bankruptcy process they invoked by seeking a share of the bankruptcy res.

[21] As this Court said long ago, in the context of upholding the Court of Claims' power to issue relief on counterclaims:

> Congress, by the act in question, informs the claimant that if he avails himself of the privilege of suing the government in the special court organized for that purpose, he may be met with a set-off, counter-claim, or other demand of the government, upon which judgment may go against him, without the intervention of a jury, if the court, upon the whole case, is of the opinion that the government is entitled to such judgment. If the claimant avails himself of the privilege thus granted, he must do so subject to the conditions annexed by the government to the exercise of the privilege.

McElrath v. United States, 102 U.S 426, 440 (1880).

adjudicating the entire dispute that his proof of claim placed at issue.[22]

2. Core jurisdiction over all compulsory counterclaims comports with historical standards and poses *de minimis* separation-of-powers concerns under the current bankruptcy law.

Schor and *Thomas* "turned to history and tradition to help define the type of adjudicatory proceeding that the Constitution reserves exclusively for Article III Courts." *Arnold Print Works*, 815 F.2d at 169 (Breyer, J.). A historical definition supports core jurisdiction over all compulsory counterclaims, since "[c]ounterclaims arising from the same transaction as the creditor's claim have also been traditionally adjudicated by non-Article III bankruptcy judges." *Beugen*, 81 B.R. at 1000; *see Marathon*, 458 U.S. at 97-100 & n.4 (White, J., dissenting) (historical discussion); *Schor*, 478 U.S. at 852; §1.A.1, *ante*.

[22] That is particularly true given that Pierce would not have been left empty-handed had he opted against filing a proof of claim. He filed both (1) a proof of claim, to obtain a recovery from Vickie's bankruptcy estate on his defamation claim, and (2) a nondischargeability complaint, to obtain a judgment against Vickie personally that would survive the bankruptcy discharge. He could have avoided core jurisdiction under §157(b)(2)(C) entirely by seeking only a nondischargeability ruling. Pierce is bound by his tactical choices.

Further, "[t]here is no constitutional right to obtain a discharge of one's debts in bankruptcy." *United States v. Kras*, 409 U.S. 434, 446 (1973). Nor is there any constitutional or common law right to file proofs of claim in bankruptcies, to request participation in bankruptcy estates, or to seek the adjustment of debtor-creditor rights. Rather, the statutory scheme of allowing debtors to obtain a discharge of debts "is a legislatively created benefit" stemming from Congress' "plenary and exclusive" power over bankruptcy. *Id.* at 447; *see also id.* (noting Congress could have delegated "to an administrative agency," rather than a court, the responsibility for processing petitions for discharge).

In light of Congress' plenary Article I power, this Court previously rejected an Article III challenge to Congress' decision to delegate to an administrative agency (the Interstate Commerce Commission) certain bankruptcy decisionmaking involving the rights of debtors and creditors in railroad reorganizations. *RFC v. Bankers Trust Co.*, 318 U.S. 163, 168-70 (1943). It recognized that there was no reason why the specialized factfinding "should not be litigated, as are other claims against bankrupt estates, by such machinery and in such manner as Congress shall prescribe. . . ." *Id.* at 170; *see id.* at 175 (Douglas, J., concurring) ("that Congress has customarily entrusted administration of the various bankruptcy acts to the courts does not mean that it must do so").

Accordingly, claims allowance and the adjustment of the debtor-creditor relationship is a scheme

of congressionally-created rights involving a specialized area where Congress has plenary Article I power. It is a distinctly federal scheme, even though the underlying bankruptcy adjudications between debtors and creditors may involve the adjustment of rights created under state law. *See Schor*, 478 U.S. at 852 (citing *RFC*, 318 U.S. 163, as upholding a non-Article III agency adjudicating state law claims that are "ancillary to a federal law dispute"); *Schor*, 478 U.S. at 856 (emphasizing that "[t]he CFTC adjudication of common law counterclaims is incidental to, and completely dependent upon, adjudication of reparations claims created by federal law"); *id.* at 853 (emphasizing that the non-Article III commission in *Schor* and non-Article III agency in *Crowell v. Benson*, 285 U.S. 22 (1932) deal "with a 'particularized area of law' ").

As the *Marathon* plurality recognized, "when Congress creates a substantive federal right, it possesses substantial discretion to prescribe the manner in which that right may be adjudicated," including requiring persons seeking to vindicate those rights to "do so before particularized tribunals created to perform the specialized adjudicative tasks related to that right," even if they perform factfinding and other "functions historically performed by judges." *Marathon*, 458 U.S. at 80-81, 83.

Core jurisdiction over all compulsory counterclaims is also appropriate in light of the concerns that motivated Congress. *See Thomas*, 473 U.S. at 587; *Schor*, 478 U.S. at 857. It promotes the expeditious

and efficient administration of claims administration and adjustment of debtor-creditor relations, considerations this Court deemed worthy in *Katchen*. *See Katchen*, 382 U.S. at 328 ("this Court has long recognized that a chief purpose of the bankruptcy laws is 'to secure a prompt and effectual administration and settlement of the estate of all bankrupts within a limited period'"); *see also Schor*, 478 U.S. at 855 (Congress authorized the CFTC to adjudicate the "same transaction" counterclaims to create "an inexpensive and expeditious" forum for claims resolution).

In addition, core compulsory-counterclaim jurisdiction is appropriate in light of the concerns that underlie Article III's tenure and salary protections – preserving "to litigants their interest in an impartial and independent federal adjudication of claims within the judicial power of the United States" and preventing the executive and legislative branches from encroaching on the judiciary. *Schor*, 478 U.S. at 850; *see id.* at 856 (concluding that under the CFTC scheme, "the magnitude of any intrusion on the Judicial Branch can only be termed *de minimis*"). Compulsory counterclaim jurisdiction poses only a *de minimis* intrusion on those interests, under the current bankruptcy law.

The 1984 Act's procedural changes diminish the threat of political-branch encroachment that undergirded much of the *Marathon* plurality's concerns. *See* §§I.A.2, I.B.1, I.B.2, *ante*; *see also Mankin*, 823 F.2d at 1309; *In re Finevest Foods, Inc.*, 143 B.R. 964, 966-71 (Bankr. M.D. Fla. 1992); *In re Jennings*, 83 B.R. 752,

759-61 (D. Nev. 1988). Under the current adjunct approach, Article III judges (instead of the political branches) control the appointment and removal of bankruptcy judges, the Article III district courts have unfettered discretion to refer or withdraw bankruptcy cases, bankruptcy judges can issue only proposed findings on matters peripherally related to the bankruptcy case (such as the debtor's claim against the non-creditor in *Marathon*), and all bankruptcy court decisions are subject to *two levels* of review by Article III courts (the district court and the circuit court), plus potential discretionary review by this Court.[23]

C. Core Jurisdiction Over All Compulsory Counterclaims To Creditor Claims Against The Estate Is Constitutional Under A "Public Rights" Or A *Crowell* Adjunct-Court Theory.

1. Public rights theory.

Although the *Marathon* plurality recognized that non-Article III judges can adjudicate "public rights," it described that doctrine as applying to matters arising "'between the government and others.'" 458 U.S. at 69. This Court has since held, however, that the doctrine applies to contexts where the federal

[23] If all parties consent, the appeal from the bankruptcy court can instead be heard by a bankruptcy appellate panel comprised of three bankruptcy judges. 28 U.S.C. §158(b)(1), (5), (c)(1). The panel's decision is appealable to the Article III circuit court. *Id.*, §158(c)(2), (d)(1).

government is not a party. *Thomas*, 473 U.S. at 585-88 (O'Connor, J., majority); *id.* at 598-600 (Brennan, J., concurring); *Granfinanciera*, 492 U.S. at 54.

In cases not involving the federal government, the test to determine whether a right is a "public right" that can be relegated to a non-Article III tribunal is whether "'Congress, acting for a valid legislative purpose pursuant to its constitutional powers under Article I, [has] create[d] a seemingly "private" right that is so closely integrated into a public regulatory scheme as to be a matter appropriate for agency resolution, with limited involvement by the Article III judiciary.'" *Granfinanciera*, 492 U.S. at 54 (quoting *Thomas*, 473 U.S. at 593-94).

The statutory process of bankruptcy courts adjudicating proofs of claim and compulsory counterclaims falls squarely within this definition. This Court effectively recognized that in *Langenkamp* when it held that there was no jury-trial right because the counterclaims to proofs of claim were "part of the claims-allowance process" and therefore "integral to the restructuring of the debtor-creditor relationship through the bankruptcy courts' equity jurisdiction." 498 U.S. at 44; *see, e.g.*, *In re Americana Expressways, Inc.*, 161 B.R. 707, 711 (D. Utah 1993) ("Although the *Granfinanciera* Court equivocated on the question whether the restructuring of debtor-creditor relations is a public right, . . . it apparently affirmed this proposition in *Langenkamp*. . . . [T]he *Langenkamp* Court implicitly recognized the restructuring of the debtor-creditor relationship through the

claims allowance process as a public right"); *Applied Thermal Sys.*, 294 B.R. at 789 ("the adjudication of counterclaims in the context of claims allowance constitutes the adjudication of public rights by the bankruptcy court").[24]

2. *Crowell* adjunct-court theory.

Expansion of the public rights doctrine beyond contexts where the federal government is a party has elicited criticism. *See, e.g., Granfinanciera*, 492 U.S. at 68-69 (Scalia, J., concurring) (arguing that the expanded version means "a purely private federally created action d[oes] not require Article III courts" and that the Court should return to requiring that the United States be a party). But that terminological battle largely stems from the conflation of adjunct-court concepts with the traditional "public rights"

[24] *See also In re Hudson*, 170 B.R 868, 873 (E.D N.C. 1994) ("by filing a claim with the bankruptcy court against the bankruptcy estate, a creditor places his dispute with the debtor into the arena of public rights"); *In re Lloyd Secs., Inc* , 156 B.R. 750, 752 (Bankr. E D. Pa. 1993) (under *Granfinanciera* and *Langenkamp*, "when a creditor presents a 'claim' against the bankruptcy estate, that creditor triggers the process of allowance and disallowance of claims, thereby . . . placing the parties' dispute into the arena of 'public rights' "); *In re Ne. Graphic Supply, Inc.*, No. 03-20069, 2003 WL 22848944, at *3 (Bankr. D. Me. 2003) ("[o]therwise legal causes of action tried in the bankruptcy court do not lose their Seventh Amendment entitlement because they are being tried in a court of equity, but rather because they are subsumed within a public rights legislative scheme for restructuring the debtor-creditor relationship").

concept that adjudications involving the federal government differ because the government can define the extent to which it waives its sovereign immunity.

In *Granfinanciera*, for example, Justice Brennan acknowledged that *Atlas Roofing*, 430 U.S. at 450 n.7, and *Crowell*, 285 U.S. at 51-65, upheld the assignment of "private rights," *i.e.*, "the liability of one individual to another under the law as defined" (*Crowell*, 285 U.S. at 51) to non-Article III adjudicators in contexts where an administrative agency or a specialized court of equity serves as a fact-finding adjunct to an Article III court. *See Granfinanciera*, 492 U.S. at 55 n.10. But he then labeled this adjunct approach as "involving statutory rights that are integral parts of a public regulatory scheme" and chose to "now refer to those rights as 'public' rather than 'private.'" *Id.*

As shown above, core jurisdiction over all compulsory counterclaims to proofs of claim fits within Justice Brennan's re-formulation of "public rights" theory. But even if one rejects that re-formulation, such core jurisdiction falls within the adjunct-court approach recognized in *Crowell*.

In *Crowell*, this Court upheld the constitutionality of a statutory scheme holding employers strictly liable in certain admiralty proceedings, under which the findings of a non-Article III commissioner, "supported by evidence and within the scope of his authority," were final as to employee injuries within the statute's purview. 285 U.S. at 46. The Court

recognized that the proceeding is "one of private right, that is, of the liability of one individual to another under the law as defined," and did not fall within any of the Court's prior categories for upholding non-Article III adjudications, including public rights cases. *Id.* at 51.

Nonetheless, it upheld the commissioner's authority to determine all "questions of fact as to the circumstances, nature, extent, and consequences of the injuries sustained by the employee for which compensation is to be made in accordance with the prescribed standards," emphasizing that the district court retained full authority over all matters of law, including determining whether evidence in the record supported the commissioner's award. *Id.* at 46-48, 54. The Court also concluded that the district court must independently determine whether the circumstances fell within the commissioner's statutorily-defined jurisdiction. *Id.* at 63-64.

Thus, as the *Marathon* plurality acknowledged, *Crowell* recognized that "with respect to congressionally created rights, some factual determinations may be made by a specialized tribunal designed by Congress," so long as an Article III court retained full authority over matters of law. *Marathon*, 458 U.S. at 80-81; *see also RFC*, 318 U.S. at 171 (upholding specialized bankruptcy-related factfinding by non-Article III commission that was only subject to "a court's supervision in matters of law").

The current bankruptcy scheme for core proceedings is analogous to the adjunct approach upheld in *Crowell*. On appeal from the bankruptcy court's judgment in a core proceeding, the district court independently reviews and decides all matters of law, including reviewing whether substantial evidence supports the bankruptcy court's findings and whether the bankruptcy court correctly concluded that core jurisdiction existed, all consistent with *Crowell*.[25]

A *Crowell* adjunct-court theory supports core jurisdiction over all compulsory counterclaims to proofs of claim, because the Article III district court retains the requisite level of control.

♦

[25] In non-core proceedings, the district court treats any bankruptcy court findings as proposed and engages in de novo review of facts, consistent with the standard that *United States v. Raddatz*, 447 U.S. 667 (1980) upheld for magistrate review.

CONCLUSION

For all the foregoing reasons, petitioner respectfully submits that the decision below should be reversed.

Dated: November 12, 2010

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RESPONDENT'S BRIEF

Supreme Court, U.S.
FILED
DEC 13 2010
OFFICE OF THE CLERK

No. 10-179

IN THE

Supreme Court of the United States

HOWARD K. STERN, EXECUTOR
OF THE ESTATE OF VICKIE LYNN MARSHALL,
Petitioner,

v.

ELAINE T. MARSHALL, EXECUTRIX
OF THE ESTATE OF E. PIERCE MARSHALL,
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ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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PRELIMINARY STATEMENT

In 1978, Congress enacted a new Bankruptcy Code, created a new system of non-Article III bankruptcy courts, and vested these courts with broad jurisdiction to hear and determine all "civil proceedings arising under title 11 [the Bankruptcy Code] or arising in or related to cases under title 11." 28 U.S.C. §1471(b) (repealed 1984). In 1982, this Court invalidated section 1471(b), at least insofar as it authorized the non-Article III bankruptcy court to finally decide a state law breach of contract action. *Northern Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 87 (1982); *see also id.* at 91 (Rehnquist, J., concurring in judgment).

In 1984, Congress responded to *Marathon* by revamping the bankruptcy jurisdictional scheme. In doing so, Congress recast bankruptcy judges as non-Article III "unit[s]" of the district court "to be known as the bankruptcy court for that district," 28 U.S.C. §151, and enacted 28 U.S.C. §§1334(b) and 157 to govern the exercise of federal bankruptcy jurisdiction.

In relevant part, section 157(b)(1) authorizes a bankruptcy judge to "hear and determine" all "core proceedings arising under title 11, or arising in a case under title 11," subject to ordinary appellate review. 28 U.S.C. §§157(b)(1), 158. In contrast, section 157(c)(1) authorizes a bankruptcy judge to "hear" a

proceeding that is "related to" a case under title 11, but not to finally decide it. *Id.* §157(c)(1). For "related to" matters, the bankruptcy judge submits proposed findings of fact and conclusions of law, subject to *de novo* review in the district court. *Id.* Further, section 157(b)(5) commands that all "personal injury tort...claims shall be tried in the district court." *Id.* §157(b)(5).

Petitioner Howard K. Stern ("Stern") contends that, prior to 1995, E. Pierce Marshall ("Pierce") tortiously interfered with an expectancy of a gift held by Vickie Lynn Marshall ("Vickie"). In 1996, Vickie filed for bankruptcy. Vickie's bankruptcy filing created her "bankruptcy estate" consisting of all of her property, including her tortious interference cause of action. 11 U.S.C. §541. Invoking section 157, Vickie pursued her state law cause of action against Pierce in the bankruptcy court.

In *Celotex Corp. v. Edwards*, this Court stated that proceedings "related to" bankruptcy include "causes of action owned by the debtor which become property of the estate pursuant to 11 U.S.C. §541." 514 U.S. 300, 307-08 n.5 (1995). The Court explained that this category of claims includes "a claim like the state-law breach of contract action at issue in [*Marathon*]." *Id.* This explanation sensibly follows the plain meaning of the text and readily encompasses Vickie's pre-existing state law tort claim—for purposes of

section 157, her state law cause of action plainly does not "arise under" the Bankruptcy Code, or "arise in" a case under the Code; it plainly arises under state law.

Stern contends that the fact that Pierce filed a proof of claim fundamentally alters the calculus. BR.16. Stern is mistaken. It is true that Pierce filed a proof of claim in Vickie's bankruptcy case for a defamation cause of action he held against her. It is also true that the filing of a proof of claim generally triggers the claims allowance process. It is not true, however, that the adjudication of state law counterclaims—even "compulsory" ones—is a necessary part of that process. The claims allowance procedure is not a broad clearinghouse for litigation by and against the debtor; it is a narrow procedure for determining a creditor's share of the debtor's bankruptcy estate. 11 U.S.C. §502.

In this case, the adjudication of Vickie's state-law tortious interference claim against Pierce does not involve determining his share of her estate under federal law; it involves resolving her cause of action against him under state law. Thus, at best, Vickie's claim is merely "related to" the administration of her estate on the theory that, if successful, it might increase the assets available for distribution. *Celotex*, 514 U.S. at 308 n.6 (explaining the concept of "related to" jurisdiction in this way).

Stern asserts that, out of administrative convenience, it is appropriate to have the bankruptcy court finally determine not only Pierce's defamation claim, but also Vickie's tortious interference claim as a compulsory counterclaim. The short answer is that the statute is not drafted that way, and Stern confuses procedure with jurisdiction. Because bankruptcy judges are not Article III judicial officers, Congress intentionally limited their ability to resolve state law causes of action that the debtor may hold against others. This does not mean that the bankruptcy court can never hear such matters. It simply means that, if the bankruptcy court hears them, it may only address them by submitting proposed findings of fact and conclusions of law (unless the parties otherwise expressly consent in writing).

It is true that there are some *federally created* causes of action that a debtor may assert against a creditor that must be adjudicated in order to resolve the creditor's claim, such as a preference action "arising under" section 547 of the Bankruptcy Code. 11 U.S.C. §547; *see also Katchen v. Landy*, 382 U.S. 323 (1966). But these causes of action are specified in section 502(d) of the Code, and Vickie's state law claim is not one of them. 11 U.S.C. §502(d).

Likewise, it may be true that there are some state law counterclaims that a debtor may assert against a creditor that are so inextricably intertwined with the creditor's claim that, as a practical matter, they must also be adjudicated in order to determine the creditor's claim. As the court below properly determined, however, Vickie's claim is not one of those, either. Pet. App. 51-55. Moreover, even if it were, the statute properly directs that the bankruptcy court may only address such matters by submitting proposed findings of fact and conclusions of law.

Cutting through all of this, a bankruptcy court is prohibited from even hearing "personal injury tort claims." Pursuant to section 157(b)(5), these may only be resolved in the district court (or an appropriate State tribunal). Because Pierce's defamation claim is such a claim, the bankruptcy court lacked jurisdiction to finally decide it, as well as Vickie's tortious interference "counterclaim."

JURISDICTION

The bankruptcy court lacked jurisdiction to decide Pierce's defamation claim, 28 U.S.C. §157(b)(5), and therefore Vickie's counterclaim. *E.g., Vaden v. Discover Bank*, 129 S. Ct. 1262, 1272 & n.10 (2009). Vickie's state law claim also does not constitute a "core proceeding[] arising under title 11, or arising in a case under title

11"; thus, the bankruptcy court could hear but not finally decide it, and was required to issue proposed findings of fact and conclusions of law. *Id.* §§157(b)(1), (c)(1). The district court had jurisdiction to vacate the bankruptcy court's final judgment. *Id.* §§1334, 158. The court of appeals had jurisdiction to affirm. *Id.* §§1291, 158. This Court has jurisdiction. *Id.* §1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The relevant constitutional provisions of Article III, the relevant jurisdictional provisions of 28 U.S.C. §§1334 & 157, and the relevant miscellaneous provisions of the Bankruptcy Code are reprinted in the appendix to this brief.

STATEMENT

1. Article III of the Constitution provides that "[t]he judicial power of the United States, shall be vested in one supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish" and that "[t]he Judges, both of the supreme and inferior Courts, shall hold their Offices during good Behaviour, and shall...receive...a Compensation, which shall not be diminished during their continuance in Office." U.S. CONST. art. III, §1. As stated in *Marathon*, "our Constitution unambiguously enunciates a fundamental principle that the 'judicial Power of the United States'

must be reposed in an independent Judiciary," and likewise "commands that the independence of the Judiciary be jealously guarded," providing, as it does, "clear institutional protections for that independence." 458 U.S. at 60 (plurality).[1]

Downplaying the commands of Article III, Stern and his *amici* contend that Congress crafted the current bankruptcy jurisdictional provisions with an eye toward administrative efficiency and, building on that theme, advocate a broad, centralized power in the bankruptcy courts to adjudicate claims having some relation to a bankruptcy case. BR.15-16; USBR.2. Administrative convenience and centralized adjudication of state law claims, however, have not been the exclusive rationale of bankruptcy jurisdiction, and in crafting the current law, Congress focused on other important values, including the principles of Article III, federalism, and fairness. *See infra* pp. 13-20; *see also Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33, 63 (1989) (quoting *Bowsher v. Synar*, 478 U.S. 714, 736 (1986)) ("[T]he fact that a given law or

[1] Under the current regime, Congress has not granted bankruptcy judges Article III status. They are appointed by the courts of appeals for fourteen-year terms. 28 U.S.C. §152(a)(1). They are subject to removal from office other than by impeachment. *Id.* §152(e). Their salaries are fixed by statute and are not immune from adjustment. *Id.* §153.

procedure is efficient, convenient, and useful in facilitating functions of government, standing alone, will not save it if it is contrary to the Constitution") (internal quotation marks omitted).

Embodying these values, the current jurisdictional scheme purposefully limits a bankruptcy court's ability to determine state law causes of action: a bankruptcy court may generally hear, but not finally decide, a debtor's state law causes of action against creditors and third parties; it may not *hear at all* state law personal injury tort claims. The principles that motivated Congress to so limit the bankruptcy court's jurisdiction have deep historical antecedents.

a. The Bankruptcy Act of 1898, Act of July 1, 1898, ch. 541, 30 Stat. 544 (repealed 1979) ("1898 Act"), conferred equitable bankruptcy jurisdiction on the federal district courts. *Id.* §2, 30 Stat. 545. The 1898 Act distinguished the district court's equitable summary jurisdiction to resolve bankruptcy administrative matters from its plenary jurisdiction to resolve legal controversies. For example, section 2(2) of the 1898 Act granted the district courts summary jurisdiction to allow and disallow claims against property within their possession. *Id.* §2(2); *Katchen*, 382 U.S. at 327. Legal controversies involving actions against creditors and other third parties, however, generally fell within the district court's

"plenary" jurisdiction, which was sharply restricted under section 23b of the Act.

Section 23b provided that "[s]uits by the trustee shall only be brought or prosecuted in the courts where the bankrupt, whose estate is being administered by such trustee, might have brought or prosecuted them if proceedings in bankruptcy had not been instituted, unless by consent of the proposed defendant." 1898 Act §23b, 30 Stat. 552; *see Bardes v. First Nat'l Bank of Hawarden*, 178 U.S. 524, 533 (1900). The purpose "was to leave such controversies to be heard and determined for the most part in the state courts, 'to the greater economy and convenience of litigants and witnesses.'" *Schumacher v. Beeler*, 293 U.S. 367, 374 (1934) (citation omitted).[2] As section 23b makes plain, Congress did not in the 1898 Act universally promote centralized adjudication in the bankruptcy court at the expense of other values.

The 1898 Act authorized the district courts sitting in bankruptcy to appoint referees for two-year terms to assist them in their administrative duties. 1898 Act §34a, 30 Stat. 555; *see Weidhorn v. Levy*, 253 U.S. 268, 270 (1920). Section

[2] In 1903 and 1910, Congress made exceptions to section 23 for certain fraudulent transfer and preference actions, which could be brought as plenary matters in the district courts. Act of June 25, 1910, 36 Stat. 840 (repealed 1979).

38a of the 1898 Act, 30 Stat. 555, authorized referees (later called "bankruptcy judges") to exercise designated portions of the district courts' summary jurisdiction, including the allowance or disallowance of claims filed against the debtor's bankruptcy estate, "subject always to a review by the [district] judge." *Id.*; *see also* 1898 Act §2a(10), 30 Stat. 546 (prescribing review procedure for order of referee). Critically, the referee's jurisdiction was summary only; the referee could not hear a plenary matter absent the defendant's consent. *See Marathon*, 458 U.S. at 79 n.31.

The scope of the district courts' equitable "summary" jurisdiction and, by extension, the referees' summary jurisdiction was never precisely defined, particularly with respect to counterclaims asserted against those who filed proofs of claim. Notably, section 2 did not expressly grant the district courts summary jurisdiction to adjudicate state law claims against those filing proofs of claim, and section 23b appeared expressly to preclude it. *See* App. 13a-18a. Without discussing the requirements of Article III, some lower courts determined that summary jurisdiction encompassed counterclaims "that would also be defenses to the [creditor's] claim." *Katchen*, 382 U.S. at 336 n.12 (citing lower court decisions); *see, e.g., Gill v. Phillips*, 337 F.2d 258, 265 (5th Cir. 1964); *Cherno v. Engine Air Serv.*, 330 F.2d 191, 193 (2d Cir. 1964). Other courts,

however, concluded that it did not, or did so only in sharply limited fashion. *See Katchen*, 382 U.S. at 326 n.1 (citing cases); *Solomon v. Allied Bldg. Credits, Inc.*, 209 F.2d 828, 831 (8th Cir. 1954); *In re Eakin*, 154 F.2d 717, 719 (2d Cir. 1946); *Metz v. Knobel*, 21 F.2d 317, 318 (2d Cir. 1927).

This Court never resolved the controversy, at least with respect to a district court's summary jurisdiction to adjudicate counterclaims based on pre-existing state law causes of action. In *Katchen*, all the Court decided was that a bankruptcy court could resolve within its summary jurisdiction (and therefore without a jury) a federal preference action asserted as an objection to a proof of claim—which type of action was *already* expressly excepted from section 23b. *See supra* note 2; *Marathon*, 458 U.S. at 79 n.31 (noting that *Katchen* did not discuss the requirements of Article III).

b. In 1978, Congress revamped the bankruptcy laws, creating a new system of non-Article III bankruptcy courts to administer them. *Id.* at 60-61 (plurality). Pursuant to section 1471(b), Congress vested bankruptcy judges with broad jurisdiction to hear and determine all "civil proceedings arising under title 11 or arising in or related to cases under title 11." 28 U.S.C. §1471(b) (1978).

In 1980, the Northern Pipeline Construction Co. ("Northern") commenced a bankruptcy case under the new regime. Northern's bankruptcy filing created a "bankruptcy estate" consisting of all of its property, including its pre-existing breach of contract cause of action against Marathon Pipe Line Co. ("Marathon"). 11 U.S.C. §541. Invoking section 1471(b), Northern pursued its state law cause of action against Marathon in the bankruptcy court. In 1982, this Court invalidated section 1471(b), at least to the extent it authorized the non-Article III bankruptcy court to finally decide Northern's state law action. *Marathon*, 458 U.S. at 87 (1982); *see also id.* at 91 (Rehnquist, J., concurring in judgment).

In *Marathon*, the Court explained that there are three exceptions to the constitutional command that the judicial power of the United States (including the power to adjudicate traditional state law causes of action) shall be exercised by Article III judges: (1) the jurisdiction traditionally exercised by courts-martial; (2) the jurisdiction exercised by the territorial courts; and (3) the resolution of "public right" controversies, such as disputes over public rights or benefits that Congress has created. *Id.* at 64-70 (plurality). Although some benefits conferred under the federal bankruptcy laws (*i.e.*, the discharge of debt) may be thought of as "public rights," the plurality explained that

these "must be distinguished from the adjudication of state-created private rights, such as the right to recover contract damages." *Id.* at 71. Such state-created rights, the plurality concluded, could not be finally heard and decided by the non-Article III bankruptcy court. Although not necessarily adopting precisely the same rationale, the concurrence agreed with this conclusion. *See id.* at 92 (Rehnquist, J., concurring).

The Court stayed its judgment until October 4, 1982 to "afford Congress an opportunity to reconstitute the bankruptcy courts or to adopt other valid means of adjudication." *Id.* at 88 (plurality). The Court later extended its stay until December 24, 1982. *Northern Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 459 U.S. 813 (1982).

c. Almost immediately after *Marathon*, Congress began work on legislation to accommodate the Court's judgment. In general, early proposals favored reconstituting bankruptcy judges as Article III judicial officers. *See, e.g.*, H.R. 6978, 97th Cong. (2d Sess. 1982) (introduced on August 12, 1982, proposing essentially to reenact section 1471(b) staffed by Article III judges); H.R. REP. NO. 97-807 at 1 (1982) (discussing H.R. 6978); App. 19a. These proposals, however, did not prevail.

On December 24, 1982, the Supreme Court's stay of its mandate in *Marathon* expired. Pending action by Congress, federal courts implemented a proposed rule promulgated by the director of the Judicial Conference (the "Emergency Rule") governing the conduct of bankruptcy proceedings. Contrary to Stern's and the Government's suggestion, the foundations for the current jurisdictional scheme do not truly lie in the Emergency Rule. BR.28; USBR.7-8. Although the rule was influential, the foundations of sections 1334 and 157 were forged more deeply from a broader series of proposals, principles, and debates.

On January 24, 1983, the Senate Subcommittee on Courts held hearings. *Bankruptcy Reform Before the Subcomm. on Courts of the Comm. on the Judiciary*, 98th Cong., 1st Sess. 1 (1983). At the hearing, attendees debated a number of competing concerns in crafting a legislative response to *Marathon*, including constitutional considerations and fairness to the parties affected. Senator Heflin cautioned that the "all-encompassing" grant of jurisdiction under the 1978 Act allowed bankruptcy courts to hear any case, arising anywhere in the country, related to a debtor's petition, whether it be a civil rights, product liability, labor-management, or divorce case. *Id.* at 3 (statement of Sen. Heflin). He worried that "[f]orum shopping may develop as a race that makes the Kentucky Derby seem slow," *id.*, and opposed broad bankruptcy jurisdiction

out of fairness to litigants drawn into the proceeding.

On February 2, 1983, the House of Representatives held hearings. *Bankruptcy Court Act of 1983: Hearing Before the Subcomm. on Monopolies and Commercial Law of the Comm. on the Judiciary*, 98th Cong., 1st Sess. 58 (1983). Edward C. Schmults, Deputy Attorney General, Department of Justice, urged granting bankruptcy judges Article III status, in part on efficiency grounds: "The appointment of Article III judges will resolve any constitutional concerns, allow the consolidated disposition of all related bankruptcy matters, and attract the highest caliber of lawyers to the bench." *Id.* at 63.

The Judicial Conference of the United States, however, supported an alternative proposal that would allow non-Article III bankruptcy judges to decide all cases "arising under Title 11," but would send all claims "related to Title 11" to the Article III district courts. *Id.* at 213-14 (statement of the Judicial Conference of the United States). The Conference pointed out that those who favored establishing Article III bankruptcy courts mainly did so because of the perceived efficiency of being able to resolve all related claims in one court. *Id.* at 214. While conceding that its proposal to send all "related to" claims to the district courts could generate "a certain amount of delay as a consequence," the Conference noted that these "related to" cases

were relatively infrequent and argued that the establishment of an entire system of separate Article III courts would be overkill. *Id.*

On April 7, 1983, S. 1013, a bill sponsored by Senators Thurmond and Heflin (and ultimately passed by the Senate) was introduced, and the Senate Judiciary Committee issued a report. S. REP. NO. 98-55 (1983). The report opposed creating Article III bankruptcy courts with broad jurisdiction over bankruptcy proceedings. *Id.* at 30. It explained that, "[w]hile the objective of consolidation of judicial proceedings within a single forum is a desirable one, this is not the overriding objective of the Nation's constitutional system of courts." *Id.* at 18. The report continued: "[t]he purpose of our constitutional institutions is not mere 'efficiency'," and "[t]he value of judicial economy is further undermined by a court system in which issues of state law are adjudicated, not by those who are experts in this law (i.e. state courts), but by Federal bankruptcy and district court judges who may be totally unfamiliar with it." *Id.* at 19. Finally, the report stated that it is also "unfair to require an individual engaged in a state law dispute, who is entitled to his day in state court and who wants to exercise such an opportunity, to have to submit to the exercise of jurisdiction by a Federal court where venue may be on the opposite side of the country." *Id.*

Summarizing its reading of *Marathon*, the report stated that "[a]bsent the consent of parties to litigation, Article III of the Constitution requires that 'traditional' state common-law actions, which are only tangentially related to a title 11 bankruptcy action, be tried before an Article III judge." *Id.* at 33. The report added further, "[t]here is serious constitutional question about the ability of Congress to establish jurisdiction in the Federal courts over causes *arising purely under State law, e.g. contract claims, property valuation, etc....*" *Id.* at 40 (emphasis added).

Following debate, the Senate passed S. 1013 on April 27, 1983, and transmitted the legislation to the House. App. 21a. On March 19, 1984, H.R. 5174 was introduced. App. 25a. As originally formulated, the language of H.R. 5174 proposed the creation of Article III bankruptcy courts with broad authority over matters affecting a bankruptcy case. App. 26a.

During debate in the House on H.R. 5174, members explained that the original jurisdictional scheme of the 1978 Act that sought to "spread the jurisdiction of the bankruptcy courts" went too far, permitting bankruptcy courts to adjudicate too much, namely "rights arising under State law." 130 CONG. REC. H6204-05 (daily ed. March 21, 1984) (statement of Rep. Kindness). Echoing the views of Senator Heflin, Representative Kastenmeier urged that

the solution to the constitutional problem was to restrict the ability of bankruptcy judges to hear state law matters and to make them non-Article III judicial officers subject to supervision by the district courts. *Id.* at H6202 (statement of Rep. Kastenmeier). These views carried the day, and the House adopted a heavily revised H.R. 5174 setting out most of the basic provisions of the current law. App. 27a.[3]

Following passage, the House sent the legislation to the Senate, which held further debate and offered additional amendments. *See, e.g.*, App. 33a, 40a. Senator DeConcini proposed an amendment to exclude personal injury tort claims from the bankruptcy courts' claims allowance authority. *See* App. 42a-43a. As he explained, "[u]nlike a trade creditor who elects to do business with a particular company, the personal injury tort claimant does not choose to be injured by a particular debtor," and therefore should "have the right to have a final order entered by an Article III district judge." 130 CONG. REC. S13076 (daily ed. May 21, 1984) (statement

[3] Although Stern and the Government cite to some of the legislative history, they ignore the proceedings in the Senate, as well as the overall evolution of the legislation, focusing instead on excerpts from the House debate on March 21, 1984. *See, e.g.*, BR.31; USBR.7-8. Among other omissions, they skip subsequent amendments adding, among other things, section 157(b)(5). *See* App. 29a-32a, 42a-45a, 50a-54a.

of Sen. DeConcini); *see also id.* at S13077 (section-by-section analysis). Senator Thurmond moved for a conference with the House to address the Senate's amendments. 130 CONG. REC. S17158-59 (daily ed. June 19, 1984) (statement of Sen. Thurmond).

On June 29, 1984, the conference issued a report that reproduced the text of an amended H.R. 5174, which included the addition from conference of section 157(b)(5) requiring personal injury tort claims to be decided in the district courts. H.R. REP. NO. 98-882 at 10 (1984); App. 52a-53a. Senator Dole explained that, under the amended bill, "[o]ne of those areas reserved for attention of the district courts will be personal injury claims, which are exempted from the definition of core proceeding under the bill." 130 CONG. REC. S20083 (daily ed. June 29, 1984) (statement of Sen. Dole). Senator Dole also stated that "[t]he result of the conference discussion was a provision that preserves the integrity of bankruptcy jurisdiction while allowing abstention for personal injury cases where they can be timely adjudicated in State courts." *Id.* Critically, he then added: "*In addition, where abstention does not occur, those cases will be handled by the district court where the bankruptcy has been filed or, if that court finds it appropriate, where the claim arose.*" *Id.* (emphasis added). Thus, as Senator Dole explained, the abstention provisions of the current law (28 U.S.C. §1334(c)) are available to channel personal injury tort litiga-

tion to the state courts. Where abstention is not appropriate, section 157(b)(5) channels personal injury tort litigation to the district courts.

2. In June of 1994, J. Howard Marshall ("J. Howard") married Vickie. ER-95, 2420.[4] Both prior to and during their marriage, J. Howard gave Vickie substantial gifts worth over $6 million. ER-2536-39, 2547-48. Two weeks after the marriage, J. Howard executed his final amended and restated living trust instrument, irrevocably fixing the terms of his living trust in a manner that left the bulk of his estate to his son, Pierce. ER-645-46, 1018, 3210, 3264-68. J. Howard died on August 4, 1995. ER-2661.

In April 1995 (several months prior to J. Howard's death), Vickie commenced proceedings in the Texas probate court (the "Probate Court"), seeking a declaration concerning the validity of the living trust and alleging that Pierce had tortiously interfered with her property rights concerning J. Howard's assets. Pet. App. 11; ER-5615-17, 5620. Vickie thereafter contested J. Howard's will in the Probate Court, challenged the validity of J. Howard's estate plan, and subsequently pursued against Pierce in the probate case her alleged state law claim for "tortious in-

[4] The term "ER" refers to certain "excerpts of record" filed in the Ninth Circuit.

terference with an expectancy of a gift" (the "Probate Case"). ER-1319-31, 2863-65, 5523-31.

For several years, Vickie participated fully in the Probate Case, litigated her tortious interference claim there, and likewise litigated all of her allegations involving J. Howard's intent and Pierce's conduct. Pet. App. 61; *Marshall v. Marshall*, 392 F.3d 1118, 1128-29 (9th Cir. 2004). In particular, prior to trial, Vickie identified the causes of action against Pierce that she proposed to try to the Texas jury, including her claim of tortious interference with a gift, ER-4073, 4076-78, 4089, 4102, later emphasizing to the jury that "[t]his is a case about tortious interference with an intent to give an *inter vivos* gift...." ER-4068, 4106, 4134. Vickie called seven witnesses in her case in chief, ER-4069-70, and three additional witnesses in rebuttal. ER-4070-71. Vickie's counsel questioned at least fourteen other witnesses. ER-4070-71. Vickie herself testified for approximately six days, including extensively regarding her alleged expectancy of a gift. ER-4071.

All told, the Probate Court heard the testimony of over forty witnesses and received hundreds of items of evidence, ER-4066-71, 4706-27, including the testimony of J. Howard's staff, family, accountants, and lawyers. Following the jury's verdict, the Probate Court entered a final

amended judgment on December 7, 2001 (the "Probate Judgment"). ER-4706, 4727.

The Probate Court specifically ruled that "[J. Howard] did not intend to give and did not give to [Vickie] a gift or bequest from the Estate of [J. Howard] or from the [living trust—which contained all of his assets] either prior to or upon his death" and "that [Vickie] does not possess any interest in and is not entitled to possession of any property within the Estate of [J. Howard] or any property [of the living trust] because of any representations, promises, or agreements." ER-4721. The Probate Court also held that (1) all of Vickie's claims were resolved and dismissed; (2) Vickie was entitled to "take nothing" from Pierce; and (3) Pierce was entitled to his inheritance free and clear of any claim by Vickie. ER-4718-19, 4721.[5]

During the course of the proceedings in the Probate Court, Vickie attempted to withdraw from the case by "non-suiting" her claims. The Probate Court, however, refused to let her withdraw, Pet. App. 20-21; *Marshall*, 392 F.3d at 1128, and Vickie thereafter participated fully as a defendant to Pierce's declaratory judgment ac-

[5] Stern inappropriately characterizes the scope of the Probate Judgment not by what it actually provides, but by snippets of statements made before it was entered. BR.7-8.

tion seeking a determination of Vickie's rights and Pierce's liabilities. Pet. App. 21 & n.19; ER-4713.[6]

As the court below concluded, all of the issues regarding J. Howard's intent to give Vickie a gift and Pierce's alleged misconduct "were fully and fairly litigated by Vickie...and Pierce...in the Texas probate court." Pet. App. 61. Further, "[d]uring the five-month trial in Texas, the jury and judge considered the evidence and arguments advanced by the parties, and the Texas probate court issued a reasoned opinion based upon the findings of fact as made by the unanimous jury." Pet. App. 61.

a. During the pendency of the probate proceedings, Vickie's lawyers made various allegedly defamatory statements about Pierce. ER-930. Subsequently, Pierce commenced a state law defamation action in Texas state court against Vickie and two of her lawyers. SER-6001.[7] After Vickie commenced her bankruptcy case, Pierce dismissed her without prejudice from the defamation suit. Pet. App. 14 n.10.

[6] Stern observes that the Bankruptcy Court enjoined Pierce from pursuing certain aspects of this litigation in the Probate Court. BR.6-7. The District Court, however, set aside that improper injunction. ER-3989.

[7] The term "SER" refers to certain "Supplemental Excerpts of Record" filed in the Ninth Circuit.

b. On January 25, 1996, while the probate and defamation proceedings were ongoing, Vickie commenced her chapter 11 bankruptcy case in the bankruptcy court in California (the "Bankruptcy Court"). ER-2642. As a result of her bankruptcy filing, the defamation action against her was stayed, *see* 11 U.S.C. §362, and Pierce therefore dismissed her "without prejudice" from the defamation action. Pet. App. 14 n.10.

By operation of law, when a debtor commences a bankruptcy case, a bankruptcy estate is formed consisting of all of the debtor's property. 11 U.S.C. §541(a)(1). Accordingly, when Vickie filed her bankruptcy case, her pre-existing state law cause of action against Pierce for tortious inference with an expectancy of a gift passed to her estate.

Under the Bankruptcy Code, a creditor holding a pre-petition claim against the debtor may file a proof of claim. *Id.* §501(a), 502(b); Fed. R. Bankr. P. 3001, 3002. Subject to exceptions not relevant here, only creditors who file proofs of claim may receive distributions from the debtor's estate. Fed. R. Bankr. P. 3002(a); *New York v. Irving Trust Co.*, 288 U.S. 329, 333 (1933). The process of the allowance of claims against the estate is governed by section 502 of the Code, which lists the relevant grounds for allowance and disallowance. 11 U.S.C. §502.

The Bankruptcy Code provides further that certain obligations that a debtor owes to a creditor are "non-dischargeable"—meaning that they pass through bankruptcy unaffected and are not extinguished. *Id.* §523. On May 7, 1996, Pierce filed a complaint to determine the nondischargeability of his defamation claim against Vickie under section 523(a)(6). JA-59. The complaint alleged that, *after* J. Howard died, Vickie's attorneys made various defamatory statements against Pierce knowing them to be false. JA-62-64. The complaint alleged that Vickie was aware of and participated in a conspiracy to make these statements. JA-65. The complaint requested a determination that Pierce's claim was non-dischargeable, but did not ask the Bankruptcy Court to decide the defamation claim itself. JA-66; Pet. App. 67-68 (Kleinfeld, J., concurring).

On June 12, 1996, Pierce filed a proof of claim form with a copy of the nondischargeability complaint attached. JA-67. In filing the form, Pierce checked the box indicating that his claim was one for a personal injury tort. JA-68; Pet. App. 78.

On June 14, 1996, Vickie filed a counterclaim to Pierce's *nondischargeability* complaint, alleging that, based on facts occurring *before* J. Howard died, J. Howard intended to give her a

substantial gift and that Pierce had interfered. ER-936, 941-45, 948-49. Vickie later objected separately to Pierce's proof of claim (listed as number 0018 in her objection), but raised no counterclaim to Pierce's proof of claim. SER-6031-32. Thus, Vickie asserted her tortious interference claim in response to Pierce's request that the bankruptcy court determine the nondischargeability of her personal liability for defamation, not in response to the defamation claim against her estate.[8]

Pierce objected to the Bankruptcy Court's assertion of jurisdiction over Vickie's claim and requested that the Bankruptcy Court abstain. *Marshall*, 392 F.3d at 1126; ER-957, 1049-69; SER-6754. Likewise, Pierce did not expressly consent in writing to the Bankruptcy Court's jurisdiction. Pet. App. 266 & n.17; Fed. R. Bankr. P. 7012(b).[9]

In September 1998, Pierce further moved to withdraw the entire litigation to the district court (the "District Court"). JA-94. As grounds for withdrawal, Pierce stated *inter alia* that his

[8] Stern's counsel conceded this point below. 9th BR-132-33 n.7 (2003).

[9] Stern incompletely characterizes Pierce's intentions concerning his proof of claim not by what Pierce filed or pled, but with brief excerpts of what Pierce or his counsel said at certain points. BR.3.

defamation claim was a personal injury tort claim and that the Bankruptcy Court lacked jurisdiction to decide it under 28 U.S.C. §157(b)(5). JA-110-12. The District Court initially granted the motion, JA-123, but later returned the matter to the Bankruptcy Court after receiving an internal memorandum from the Bankruptcy Court. JA-138-39.[10]

On March 5, 1999, while Vickie's counterclaim for tortious interference remained pending, Vickie confirmed her chapter 11 plan and received a discharge of her debts. ER-2200-02. On November 5, 1999, the Bankruptcy Court granted Vickie's motion for summary judgment on Pierce's nondischargeability complaint. ER-2756-58. Instead of resolving the narrow bankruptcy question of nondischargeability, the court summarily determined that Vickie had no liability for any defamatory conduct and that Pierce had no claim. ER-2757. Significantly, the resolution of Vickie's tortious interference claim

[10] On January 12, 1999, the bankruptcy judge stated his intent to submit a memorandum to the district court "to assist in his review of the matter" and that the contents would not be "available to the parties." ER-2158. In a subsequent hearing, the district judge acknowledged receiving the memorandum, stating that "as far as the memorandum that he shared with me, he does have the authority to try everything [other than a separate lawsuit not at issue in this proceeding]." JA-128.

played no part in the allowance or disallowance of Pierce's claim. Following her bankruptcy discharge and the subsequent summary resolution of Pierce's underlying defamation claim, Vickie litigated her tortious interference claim against Pierce in both the Bankruptcy Court and the Probate Court.

c. On October 25, 1999, the Bankruptcy Court commenced hearings on Vickie's tortious interference claim. Over five days of hearings, the Bankruptcy Court severely circumscribed Pierce's presentation of evidence and made findings of fact adverse to him as a sanction for alleged discovery abuses that remain strenuously disputed. ER-2173-75, 2641-49.[11] The Bankruptcy Court had previously entered its sanctions order against Pierce on February 2, 1999. As the Court of Appeals explained, "[t]he sanctions imposed by the court deemed almost all facts alleged in the pleadings filed by the attorneys for Vickie...to be admitted facts...." *Marshall*, 392 F.3d at 1126. In addition, "[a]s a re-

[11] Contrary to Stern's statements, BR.4-5 nn.4-5, Elaine, Pierce's widow, contends that Pierce did not destroy any documents relevant to Vickie's claim, that he did not fail to produce critical documents, and contests Stern's other allegations of discovery abuse—none of which have been resolved on appeal, apart from the District Court's initial vacatur of the Bankruptcy Court's sanctions as not supported by the record, discussed *infra*.

sult of the sanctions order, [Pierce] was not allowed to present conflicting evidence...." *Id.* at 1127; Pet. App. 19 n.17.

Pierce appealed the sanctions order to the District Court. On March 9, 1999, the District Court vacated the sanctions order, finding that the order was not supported by the record. ER-2211-12, 5744-49. On remand, and without taking evidence, the Bankruptcy Court reimposed its sanctions order. ER-2240.

On January 18, 2000, "the bankruptcy court *sua sponte* withdrew its sanctions order, but did not change any of its other rulings which had been based on the allegations by Vickie...deemed true." *Marshall*, 392 F.3d at 1127. In doing so, the Bankruptcy Court "did not hold another evidentiary hearing." *Id.*

On September 27, 2000, nearly a year after it summarily resolved and dismissed Pierce's underlying defamation claim, the Bankruptcy Court determined that Vickie had an expectancy of an inheritance, based on a "widow's election" theory, and awarded Vickie $449,754,134. Pet. App. 18; ER-3031-38. On October 6, 2000, the Bankruptcy Court *sua sponte* issued a revised opinion, abandoning its "widow's election" theory and deeming that Vickie had an expectancy of a substantial portion of J. Howard's wealth. Pet. App. 19; ER-3047-55. Concluding on the basis of

presumed facts imposed as a sanction that Pierce interfered with this expectancy, the court again awarded Vickie $449,754,134. On November 21, 2000, the Bankruptcy Court assessed punitive damages against Pierce in the amount of $25 million and, on December 29, 2000, entered judgment in Vickie's favor for approximately $475 million (the "Bankruptcy Judgment"). ER-3360.

In its opinion of December 29, 2000, the Bankruptcy Court concluded that it had jurisdiction to enter the Bankruptcy Judgment, rejecting Pierce's argument that the "probate exception" to federal jurisdiction applied. Pet. App. 286-99. In addition, the court concluded that Vickie's claim for "tortious interference" constituted a counterclaim to Pierce's defamation claim and, thus, a "core" bankruptcy proceeding under 28 U.S.C. §157(b)(2)(C). ER-306-07.

d. Pierce appealed the Bankruptcy Judgment to the District Court. On June 20, 2001, the District Court affirmed the Bankruptcy Court's determination that the "probate exception" did not apply, but reversed the Bankruptcy Court's conclusion that Vickie's tortious interference claim constituted a "core" proceeding that the Bankruptcy Court could finally resolve and vacated the Bankruptcy Judgment. Pet. App. 283. The District Court concluded that Vickie's claim was not "core" because it was only "some-

what related" to Pierce's defamation claim, and Pierce was entitled to an adjudication of Vickie's allegations in an Article III forum. Pet. App. 283.

Following vacatur of the Bankruptcy Court's decision, Pierce moved in the District Court to dismiss Vickie's "tortious interference" counterclaim on the grounds that it was barred by the doctrines of claim and issue preclusion following the Probate Court's final judgment. Pet. App. 222-23. The District Court denied the motion. Pet. App. 234.

Asserting its own bankruptcy jurisdiction, the District Court conducted a "*de novo*" review of Vickie's "tortious interference" claim. Like the Bankruptcy Court, the District Court refused to hear many of Pierce's percipient witnesses, Pet. App. 63 n.33, but heard all of Vickie's witnesses. ER-5280-87. On March 7, 2002, the District Court ultimately awarded Vickie $88,585,534.66 on her claim (the "District Court Judgment"), concluding that J. Howard's signature on the Trust was forged; that the estate plan did not reflect J. Howard's true intentions; and that Pierce had thwarted J. Howard's intent to give Vickie an alleged gift by engaging in illegitimate "estate planning transactions for J. Howard," Pet. App. 90-214, 215-16, conclusions diametrically opposed to the determinations of the Probate Court

and, Pierce argued, unsupported by any evidence.

The District Court did not reach the issue whether Pierce committed discovery abuse and declined to consider the Bankruptcy Court's sanctions rulings. Pet. App. 98-99. Accordingly, the merits of the sanctions order and the Bankruptcy Judgment on which it was based have never been reviewed on appeal, the District Court having vacated the Bankruptcy Judgment on jurisdictional grounds.

Prior to conducting its own hearings, the District Court ordered a complete "redo" of discovery that included turning over to Vickie's counsel not only all of the relevant documents, but also all of Pierce's privileged communications with his attorneys, ER-4063, including the privileged document between Pierce and his counsel that Stern has reproduced in the Joint Appendix. JA-53. Pierce appealed the District Court Judgment to the Court of Appeals.

e. In vacating the District Court Judgment, the Ninth Circuit first held that the "probate exception" applied in this matter. *Marshall*, 392 F.3d at 1137. This Court subsequently reversed that determination. *Marshall v. Marshall*, 547 U.S. 293 (2006). Following remand, the principal parties died. Stern assumed responsibility for pursuing the interests of Vickie's

estate. Elaine, Pierce's widow, assumed responsibility for pursuing the interests of Pierce's estate.

In the decision below, the Ninth Circuit held that Vickie's counterclaim to Pierce's nondischargeability complaint was not a "core" bankruptcy proceeding arising in a bankruptcy case because her counterclaim was "not so closely related to Pierce Marshall's defamation claim that it must be resolved in order to determine the allowance or disallowance of his claim against her bankruptcy estate." Pet. App. 51. Accordingly, because it resolved a "related to" matter, the Bankruptcy Judgment properly constituted merely *proposed* findings of fact and conclusions of law subject to "*de novo*" review in the District Court, and not a final judgment. *See* Fed. R. Bankr. P. 9033. In contrast, the Probate Judgment was properly a final judgment. Because the Probate Judgment preceded the District Court Judgment and resolved issues dispositive of Vickie's "tortious interference" claim, the Ninth Circuit applied the doctrine of issue preclusion and held that the earlier final Probate Judgment prevented Vickie from succeeding on her claim for tortious interference in the District Court. (Stern did not seek review of the court's preclusion determination.) Pet. App. 55-57.

Judge Kleinfeld filed a concurring opinion "to offer additional grounds that compel the

same result," Pet. App. 66, including that the Bankruptcy Court lacked jurisdiction over Pierce's defamation claim, and likewise Vickie's counterclaim, because both constituted personal injury tort claims. Pet. App. 74-75.

In resolving this case on jurisdictional and preclusion grounds, the court below did not address several issues raised, briefed, and argued, including (1) whether Vickie's claim was barred by the Texas statute of frauds; (2) whether Pierce's due process rights were violated; (3) whether there is any evidence to support Vickie's claim that Pierce engaged in wrongdoing; (4) whether bankruptcy jurisdiction existed over Vickie's claim given that she had no unpaid creditors and the outcome of the litigation over her claim could benefit no one other than her; (5) whether Texas recognizes a cause of action for tortious interference with an expectancy of a gift and, if so, what are its elements; (6) whether Vickie's claim is barred by doctrines of issue and claim preclusion, including the "last-in-time" rule; and (7) whether jurisdiction in the Bankruptcy Court was precluded because Pierce's claim is a personal injury tort claim. In addition, although Pierce appealed the Bankruptcy Judgment to the District Court on a variety of grounds, the District Court reached only the jurisdictional issues discussed above, leaving the others unresolved, including the merits of the sanctions orders. These issues remain open. *See*

United States v. O'Hagan, 521 U.S. 642, 678 (1997).

SUMMARY OF THE ARGUMENT

Vickie's alleged cause of action for tortious interference with an expectancy of a gift is a claim that pre-dates her bankruptcy and arises under state law. Adhering to the requirements of Article III, the principles of *Marathon* and *Celotex*, and likewise the express provisons, history, and purposes of the governing statutory scheme, Vickie's state law claim is, at best, a "related to" matter, and the decision below should be affirmed.

First, the adjudication of Vickie's state law claim in federal court requires the exercise of the federal judicial power. Under the provisions of Article III, that power must be exercised by a federal judge with the guarantees of lifetime tenure and irreducible salary. None of the recognized exceptions to that requirement apply in this case. As a bankruptcy matter, it was not necessary for the Bankruptcy Court to finally decide Vickie's claim in order to allow or disallow Pierce's proof of claim. Consistent with the requirements of Article III, the Bankruptcy Court could not finally "hear and determine" Vickie's claim.

Second, when Congress created the current statutory scheme, it did so to comply with the requirements of *Marathon*, and likewise to promote federalism and fairness to non-debtor litigants. Consistent with these values, Congress purposefully limited the bankruptcy courts' jurisdiction in section 157(b)(1) to "core proceedings arising under title 11, or arising in a case under title 11." Under a plain reading of this provision, a debtor's state law cause of action that exists prior to bankruptcy does not fall within its scope. Among other reasons, such an action does not "arise under" the Bankruptcy Code, or "arise in" a case under the Code; it arises under state law. Further, the fact that the debtor asserts the state law claim as a "counterclaim" to a proof of claim does not alter the analysis, especially where, as here, it is not necessary to adjudicate the debtor's claim in order to allow or disallow the creditor's proof of claim. Applying these principles in this case, Vickie's state law claim constitutes a "related to" matter that the Bankruptcy Court could "hear" and address only by submitting proposed findings of fact and conclusions of law, subject to *de novo* review in the district court.

Finally, Congress explicitly provided that all "personal injury tort...claims shall be tried in the district court." 28 U.S.C. §157(b)(5). Pierce's defamation claim is a personal injury tort claim within the meaning of this provision. Given that

the bankruptcy court could not decide Pierce's defamation claim *at all*, there is no basis for the conclusion that the Bankruptcy Court, for efficiency or other reasons, should have decided Vickie's tortious interference claim as a "counterclaim" to Pierce's claim.

ARGUMENT

I. The Constitution Bars a Non-Article III Bankruptcy Court from Finally Adjudicating a State Law Counterclaim Where the Adjudication Is Not Necessary to the Claims Allowance Process.

A. Stern and his *amici* contend that 28 U.S.C. §157(b)(2) authorizes a non-Article III bankruptcy judge to hear and finally determine a debtor's state-law counterclaim against any creditor filing a claim against the estate, subject only to ordinary appellate review. That interpretation is contrary to Article III. In addition, because it raises serious constitutional questions, it should be avoided. *See Crowell v. Benson*, 285 U.S. 22, 62 (1932).

Vickie's counterclaim against Pierce alleged that he tortiously interfered with her expectancy of an *inter vivos* gift. To the extent Texas law recognizes this cause of action at all, it is a classic common-law tort. *See In re Marshall*,

275 B.R. 5, 50-51 & n.43 (C.D. Cal. 2002). This sort of state-law action between two private parties is a "private right" controversy sheltered at the heart of Article III.

In *Murray's Lessee v. Hoboken Land & Improvement Co.*, this Court acknowledged the existence of a class of cases "involving public rights" that "[C]ongress may or may not bring within the cognizance of the courts of the United States, as it may deem proper." 59 U.S. (18 How.) 272, 284 (1856). The Court emphasized, however, that Congress may *not* "withdraw from judicial cognizance any matter which, from its nature, is the subject of a suit at the common law, or in equity, or admiralty." *Id.* The Constitution requires that such matters of private right be decided by Article III judges.

Since *Murray's Lessee*, the Court has refined the boundaries of the "public rights" exception. Some cases have stated that "a matter of public rights must at a minimum arise 'between the government and others.'" *Marathon*, 458 U.S. at 69 (plurality) (quoting *Ex Parte Bakelite Corp.*, 279 U.S. 438, 451 (1929)). More recently, the Court rejected the conclusion "that the right to an Article III forum is absolute unless the Federal Government is a party of record." *Thomas v. Union Carbide Agric. Prods. Co.*, 473 U.S. 568, 586 (1985). Instead, the Court recognized that, in rare cases, Congress "may create a seem-

ingly 'private' right that is so closely integrated into a public regulatory scheme as to be a matter appropriate for agency resolution with limited involvement by the Article III judiciary." *Id.* at 594.

The Court has made clear, however, that even this broadened category of "public rights" captures only rights created by Congress. As the Court explained in its most recent discussion of the issue, "[t]he crucial question, in cases not involving the Federal Government, is whether Congress, acting for a valid legislative purpose pursuant to its constitutional powers under Article I, has created a seemingly 'private' right that is so closely integrated into a public regulatory scheme as to be a matter appropriate for agency resolution with limited involvement by the Article III judiciary." *Granfinanciera*, 492 U.S. at 54 (brackets and internal quotation marks omitted).

The Court has also made clear that "if a statutory cause of action...is not a 'public right'" under this standard, "then Congress may not assign its adjudication to a specialized non-Article III court lacking the essential attributes of the judicial power." *Id.* at 53 (internal quotation marks omitted). And it has likewise emphasized that suits between private parties arising under state common law are paradigmatic cases of "private right" in which the parties have a right to a decision by an Article III tribunal. *See*

Marathon, 458 U.S. at 70 (plurality); *id.* at 90 (Rehnquist, J., concurring in judgment). As the Court has since reiterated, *Marathon* stands for the proposition that "Congress may not vest in a non-Article III court the power to adjudicate, render final judgment, and issue binding orders in a traditional contract action arising under state law, without consent of the litigants, and subject only to ordinary appellate review." *Thomas*, 473 U.S. at 584. Because Vickie's claim against Pierce for tortious interference is a paradigmatic private-right legal dispute, it is precisely the kind of claim that may not be decided by a non-Article III tribunal.

B. In light of *Marathon* and *Granfinanciera*, it is clear that if Pierce had not filed a claim against Vickie's estate, her common-law claim for tortious interference with an *inter vivos* gift could not be decided constitutionally by a non-Article III tribunal. Neither Stern nor the Government appears to dispute this proposition. Instead, they contend that Pierce's filing of a proof of claim somehow converts Vickie's counterclaim into a matter of public right or otherwise alters the constitutional calculus. Their arguments are unsound.

Stern and the Government rely heavily on *Katchen v. Landy*, 382 U.S. 323 (1966), and *Langenkamp v. Culp*, 498 U.S. 42 (1990). BR.41-49; USBR.24-28. Those cases held that a creditor

that asserts a claim against a bankruptcy estate has no right to a jury trial on the estate's counterclaim to recoup a preferential transfer to that creditor, even though the creditor would have been entitled to a jury in the preference dispute had it not asserted a claim in bankruptcy.

But the preference counterclaims at issue in *Katchen* and *Langenkamp* differ from the counterclaim at issue here in a crucial respect: They were integral to the claims allowance process because relevant provisions of both the 1898 Act at issue in *Katchen* and the Bankruptcy Code at issue in *Langenkamp* required that the preference claim be decided and any money owed by the creditor returned before the creditor's claim could be allowed. The common-law counterclaim at issue here, of course, is entirely different. Because there was no need to adjudicate Vickie's counterclaim for tortious interference in order to resolve Pierce's proof of claim—and because Vickie's claim against Pierce is an archetypal state-law tort claim that has nothing to do with bankruptcy law or procedures—the Bankruptcy Court lacked jurisdiction to enter final judgment on Vickie's claim.

As *Katchen* explained, the 1898 Act's provisions regarding preferences "contain[ed] an[] important congressional directive around which much of this case turns." 382 U.S. at 330. Specifically, §57(g) of the Bankruptcy Act "forb[ade]

the allowance of a claim when the creditor has 'received o[r] acquired preferences...void or voidable under this title,' absent a surrender of any preference." *Id.* Thus, "[u]navoidably and by the very terms of the Act, when a bankruptcy trustee presents a §57, sub. g objection to a claim, the claim can neither be allowed nor disallowed until the preference matter is adjudicated." *Id.* Likewise, the current law provides the same rule. *See* 11 U.S.C. §502(d).

Vickie's counterclaim against Pierce, however, is not a federally-created preference action, and there was no need to decide it in order to determine whether or not to allow Pierce's claim against the estate. (In fact, the Bankruptcy Court actually resolved Pierce's claim nearly a year before it decided Vickie's counterclaim.) Accordingly, the resolution of the counterclaim at issue here simply was not "part and parcel of the allowance process," *Katchen*, 382 U.S. at 330, as in *Katchen* and *Langenkamp*.

Likewise, the resolution of Pierce's claim against the estate did not fully decide Vickie's counterclaim—in fact it did not resolve it at all. This is not surprising, given that the allowance or disallowance of claims involves a process conducted within the parameters of section 502 of the Code, which does not require (or necessarily permit) the determination of all counterclaims—even compulsory ones—in order to allow or

disallow a claim. 11 U.S.C. §502; *see Travelers Cas. & Sur. Co. v. Pacific Gas & Elec. Co.*, 549 U.S. 443, 449-50 (2007) (discussing the operation of section 502). As this Court has explained, a proof of claim "must" be allowed, unless one of the enumerated grounds for disallowance set forth in section 502(b) exists. *Id.* at 449 ("even where a party in interest objects, the court 'shall allow' the claim 'except to the extent that' the claim implicates any of the nine exceptions enumerated in §502(b)"). Significantly, the enumerated list in section 502(b) does *not* include as a ground for disallowance the fact that the debtor holds a tort claim against the creditor.[12] Thus, for purposes of section 502, Vickie's tortious interference claim was neither procedurally nor substantively relevant to (let alone intertwined with) the allowance or disallowance of Pierce's claim. In addition, because it involved vastly different and more complex factual and legal elements, the resolution of Vickie's counterclaim required the adjudi-

[12] Section 502(b) prescribes a list of defenses that may be asserted in opposition to a proof of claim, including defenses demonstrating the "unenforceability" of a claim under section 502(b)(1) (*e.g.*, a statute of limitations defense). *See* 4 COLLIER ON BANKRUPTCY ¶502.03[2][b] at 502-21 (16th ed. 2010) (discussing section 502(b)(1)). The fact that the debtor holds a claim for money damages against the creditor is not such a defense.

cation of a far broader bundle of issues. *See* Pet. App. 51-55.

Stern and the Government seek to minimize the fundamental aspects of *Katchen* (and the current law) described above, preferring instead to focus on the Court's statement, quoting *Alexander v. Hillman*, 296 U.S. 222, 241 (1935), that "[b]y presenting their claims [the claimants against the estate] subjected themselves to all the consequences that attach to an appearance." *Katchen*, 382 U.S. at 335. They also place great weight on *Katchen*'s statement that its result was "in harmony with the rule generally followed by courts of equity that, having jurisdiction of the parties to controversies brought before them, they will decide all matters in dispute and decree complete relief." *Id.*

Reliance on these very general statements, however, begs the questions of *what* consequences attach to an appearance in bankruptcy court, and *what* controversy was brought before the Bankruptcy Court in this case. *Katchen*'s ultimate holding on when bankruptcy courts may decide counterclaims consistent with the Seventh Amendment is quite specific. *Katchen* leaves no doubt that its Seventh Amendment holding extends *only* to counterclaims (*e.g.*, preference actions) that must necessarily be decided in order to complete the claims allowance process—not to any counterclaim that happens to

arise out of the same transaction as the creditor's claim. The Court confirmed this interpretation in *Granfinanciera*, explaining that "[o]ur decision [in *Katchen*] turned...on the bankruptcy court's having 'actual or constructive possession' of the bankruptcy estate, and its power and obligation to consider objections by the trustee *in deciding whether to allow claims against the estate.*" 492 U.S. at 57 (emphasis added). In this case, it was not necessary to decide Vickie's claim in order to allow or disallow Pierce's claim. Accordingly, *Katchen* provides no support for Stern's analysis—on the contrary, it supports the analysis of the court of appeals.

C. Stern next argues that by choosing to file a claim against Vickie's estate, Pierce effectively waived his right to an Article III tribunal. BR.51-55. This claim is meritless. To be sure, this Court has held that, under certain circumstances, a party can waive his personal rights under Article III. In *Commodity Futures Trading Comm'n v. Schor*, the Court concluded that a party waived his right to have an Article III tribunal decide a counterclaim against him when he "elect[ed] to forgo his right to proceed in state or federal court on his claim" and instead proceeded in an administrative tribunal within the Commodity Futures Trading Commission. 478 U.S. 833, 849 (1986). The Court concluded that by filing his claim before the CFTC, "Schor effectively agreed to an adjudication by the CFTC of

the entire controversy," including counterclaims, in that forum. *Id.* at 850.

Stern seeks to extend the reasoning of *Schor* to this case, but fails to note that *Schor* differed from this case in a critical respect: As the Court emphasized, "Schor *had the option of having the common law counterclaim against him adjudicated in a federal Article III court*, but...chose to avail himself of the quicker and less expensive procedure Congress had provided him." 478 U.S. at 850 (emphasis added).

No similar justification applies in this case because there was no other forum in which Pierce could have pursued his claim against Vickie. He was required to file a claim in bankruptcy if he wished to secure his right to a pro rata share of her estate. Indeed, this Court recognized precisely this feature of bankruptcy in *Granfinanciera*: "[In *Schor*] [t]he investors could have pursued their claims, albeit less expeditiously, in federal court. By electing to use the speedier, alternative procedures Congress had created, the Court said, the investors waived their right to have the state-law counterclaims against them adjudicated by an Article III court. *Parallel reasoning is unavailable in the context of bankruptcy proceedings, because creditors lack an alternative forum to the bankruptcy court in which to pursue their claims.*" *Granfinanciera*,

492 U.S. at 59 n.14 (emphasis added) (citation omitted).[13]

D. Stern and the Government also argue that, in light of the changes made in the 1984 amendments, the bankruptcy court's exercise of jurisdiction over Vickie's counterclaim can be justified based on the "adjunct" theory rejected in *Marathon*. BR.61-64; USBR.30-32. That argument should be rejected for several reasons.

First, to comply with Article III, "the functions of the adjunct must be limited in such a way that 'the essential attributes' of judicial power are retained in the Art. III court." *Marathon*, 458 U.S. at 81 (plurality) (quoting *Crowell*, 285 U.S. at 51). It cannot be said that the "essential attributes" of judicial power are maintained in the district court when the bankruptcy court decides state-law matters of private right under §157(b)(1)'s provisions for "core proceedings" "arising under" the Bankruptcy Code, or

[13] Stern asserts that Pierce "could have avoided core jurisdiction...by seeking only a nondischargeability ruling" rather than filing a claim against the estate as well. BR.55 n.22. But this is no answer, because a nondischargeability ruling only preserves the possibility of a future recovery against the debtor's post-bankruptcy assets, if any. Filing a claim in bankruptcy is the means by which a creditor can pursue its right to a share of the bankruptcy estate.

"arising in" a case under the Code. Most obviously, in such proceedings, bankruptcy courts are empowered to enter final judgments, which is the paradigmatic attribute of the judicial power. *Plaut v. Spendthrift Farm, Inc.*, 514 U.S. 211, 219 (1995) ("[A] 'judicial Power' is one to render dispositive judgments." (internal quotation marks omitted)).

Moreover, the bankruptcy court's determinations are subject only to ordinary appellate review. As Justice Rehnquist explained in *Marathon*, "the bankruptcy court is not an 'adjunct' of either the district court or the court of appeals" when it can resolve "[a]ll matters of fact and law in whatever domains of law to which the parties' dispute may lead ..., with only traditional appellate review by Art. III courts." 458 U.S. at 91 (Rehnquist, J., concurring). The same conclusion follows here. *See United States v. Raddatz*, 447 U.S. 667, 683 (1980) (upholding the Magistrates Act against an Article III challenge because in matters delegated to magistrate judges, "the ultimate decision is made by the district court").

Second, and more fundamentally, even Stern acknowledges that *Crowell*'s adjunct theory allows a non-Article III body to make factual determinations only "with respect to *congressionally created rights*." BR.63 (quoting *Marathon*, 458 U.S. at 80-81 (emphasis added)). Vickie's alleged right to recover for tortious in-

terference with an *inter vivos* gift, however, is a creation of state law, not federal statute. Thus, the full protections of Article III apply. *See Marathon*, 458 U.S. at 83-84 (plurality). As a result, the bankruptcy court's entry of final judgment on Vickie's tortious interference claim cannot be justified on an "adjunct" theory.

II. The Bankruptcy Court Could Not Finally Hear and Determine Vickie's State Law Counterclaim Under Section 157.

A. It is evident that Congress enacted the provisions of the current bankruptcy jurisdictional scheme in response to *Marathon* and in an effort to comply with its requirements. It is also evident that, in enacting section 157, Congress rejected proposals calling for an Article III bankruptcy court with broadly expansive jurisdictional reach. In opting for bankruptcy tribunals with more modest authority, Congress eschewed administrative efficiency and centralized adjudication as the exclusive goals of its legislative solution and embraced not only the requirements of Article III, but also values of federalism and fairness in crafting the various subparts and mechanisms of sections 1334 and 157. These provisions should be interpreted in this light.

In fleshing out its design, Congress further elected to create a stututory structure superintended by three jurisdictional concepts, namely jurisdiction over proceedings "arising under" the Bankruptcy Code; proceedings "arising in" bankruptcy cases; and proceedings "related to" such cases. Congress vested the district courts with this jurisdiction in section 1334(b) and then authorized the delegation of this jurisdiction to the bankruptcy courts in section 157(a). Because these three concepts of "arising under," "arising in," and "related to" are so obviously foundational, it is not surprising that this Court has stated that a bankruptcy court's jurisdiction "must be based on the 'arising under,' 'arising in,' or 'related to' language of §§1334(b) and 157(a)." *Celotex*, 514 U.S. at 307.

Structurally, Congress then divided this tripartite jurisdictional system into two branches. First, it authorized bankruptcy judges to finally "hear and determine" all "core proceedings arising under title 11, or arising in a case under title 11," subject to ordinary appellate review. 11 U.S.C. §§157(b)(1), 158. Second, it authorized bankruptcy judges to "hear" proceedings that are "related to" a case under title 11, but not to finally decide them. *Id.* §157(c)(1).

In creating the first branch, Congress introduced a new concept that does not appear in

section 1334(b) or 157(a)—the phrase "core proceedings." Congress defined the phrase "core proceedings" in section 157(b)(2) to include a nonexhaustive list of matters. Some of these are fairly limited and specific, such as "proceedings to determine, avoid, or recover preferences." *Id.* §157(b)(2)(F). Others, however, are open-ended, such as "matters concering the administration of the estate," *id.* §157(b)(2)(A); and "other proceedings affecting the liquidation of the assets of the estate or the adjustment of the debtor-creditor...relationship," *id.* §157(b)(2)(O). By themselves, these open-ended authorizations threaten to vest an exceptionally sweeping jurisdiction in the bankruptcy courts. But it is obvious from the overall structure of the statute that Congress intended the "arising under" and "arising in" concepts to impose some restraint on their reach. Among other reasons, section 157(b)(1) does not confer jurisdiction simply over "core proceedings"; it confers it over "core proceedings" that "arise under" the Code, or that "arise in" a case under the Code.

Ignoring the "arising under" and "arising in" language, Stern contends that the Bankruptcy Court possessed jurisdiction to finally decide Vickie's tortious interference claim exclusively by reference to section 157(b)(2)(C), which includes as an example of "core proceedings" "counterclaims by the estate against persons filing claims against the estate."

Id. §157(b)(2)(C). *See* BR.14. Stern asserts that Vickie's tortious interference claim falls within the scope of this provison as a "compulsory counterclaim," and that "Pierce forced Vickie to file her compulsory counterclaim in the bankruptcy by filing his proof of claim for defamation." BR.14. Stern contends further that, by filing his proof of claim, Pierce triggered the claims-allowance process, thereby "acquiesc[ing] to the adjudication of integrally-related counterclaims." BR.16.

Stern's argument contains several legal errors. At the outset, however, his factual contentions require qualification. Vickie did not file her tortious interference claim as a counterclaim to Pierce's proof of claim. Although she objected to his claim (listed as claim number 0018 in her pleading), she did not assert her tortious interference counterclaim in her objection. *See* SER-6030-31. In addition, her tortious interference counterclaim played no part in the allowance or disallowance of Pierce's proof of claim, which was disposed of separately long before the Bankruptcy Court decided her tortious interference claim. ER-2757.

Stern contends that "the counterclaim arose out of the same transaction that Pierce placed at issue by seeking a distribution from the bankruptcy estate." BR.14. This factual assertion also requires qualification. The

"transaction" underlying Pierce's claim is Vickie's alleged responsibility for her attorneys' defamatory statements made *after* J. Howard died on August 4, 1995. JA-59-66. In contrast, the "transaction" underlying Vickie's tortious interference counterclaim is Pierce's alleged interference with a gift *before* J. Howard passed away. ER-941-45, 948-49. The only connection between the two sets of circumstances is Stern's contention that the proof of certain facts alleged in Vickie's counterclaim could have been asserted as a "truth" defense to the defamation claim. BR.14. But Vickie did not actually object to Pierce's proof of claim on this basis.

Instead, Vickie asserted her tortious interference claim as a counterclaim to Pierce's nondischargeability complaint. This complaint, of course, was not a claim against Vickie's bankruptcy estate. It was a complaint to determine whether her personal liability for defamation would survive her bankruptcy discharge. *See* 11 U.S.C. §523; *Kawaauhua v. Geiger*, 523 U.S. 57, 60-62 (1998) (discussing nondischargeability requirements under section 523(a)(6)). Stern's factual predicates thus do not support his legal theory.

Stern's legal theory of "acquiesc[ing] to" jurisdiction is itself also unsound. At bottom, Stern seeks to elevate a procedural device jurisdiction over "compulsory counterclaims"—

into a statutory authorization that section 157 does not condone. Although section 157(b)(2) defines core proceedings to include "counterclaims" against "persons filing claims against the estate," section 157(b)(1) confers jurisdiction only over such counterclaims that "arise under" the Code, or "arise in" a case under the Code. By ignoring these provisions, Stern misses an indispensible part of the statute.

Stern's theory is misplaced for another reason. As the court below explained, "[t]he test for compulsory counterclaims is generous and designed to promote judicial efficiency by avoiding multiplicity of lawsuits." Pet. App. 49-50; *see also, e.g.*, *Southern Constr. Co. v. Pickard*, 371 U.S. 57, 60 (1962). As explained above, however, judicial efficiency was not Congress' guiding concern in circumscribing the jurisdiction of the bankruptcy courts in *Marathon*'s wake. As a result, section 157 has a narrower focus. *See* Pet. App. 50 (explaining that section 157 "is much narrower because it is designed to comply with the constitutional limitations on the bankruptcy court's jurisdiction as set forth in *Marathon*."). Likewise, the claims allowance process has a narrower focus and does not supply a procedural vehicle to ventilate counterclaims like Vickie's tortious interference claim.

B. Although section 157 does not define the phrases "arising under" or "arising in," they have developed a generally accepted meaning that excludes Vickie's pre-existing state law claim from the scope of section 157(b)(1) and renders her claim, at most, a "related to" proceeding. The common understanding of the phrase "arising under" is that it encompasses causes of action created by the Bankruptcy Code. Pet. App. 40 (citing cases); *see In re Wood*, 825 F.2d 90, 96-97 (5th Cir. 1987) ("Congress used the phrase 'arising under [the Bankruptcy Code]' to describe those proceedings that involve a cause of action created or determined by a statutory provision of [the Code]."). The common understanding of the phrase "arising in" is that it encompasses matters that are "not based on any right expressly created by title 11, but nevertheless, would have no existence outside of bankruptcy." Pet. App. 40-41 (citing cases) (citations and internal quotation marks omitted); *see also Wood*, 825 F.2d at 96-97 ("'arising in' proceedings are those that are not based on any right expressly created by [the Bankruptcy Code], but nevertheless, would have no existence outside of the bankruptcy."). Vickie's tortious interference claim obviously falls outside the scope of these standards; it is a creation of state law that could be brought in a court outside of bankruptcy.

But even if the Court were to conclude that the phrases "arising under" and "arising in" do not encompass these precise boundaries, it is still clear that they cannot include Vickie's tortious interference claim, which so plainly "arises under" state law. *See* S. REP. NO. 98-55, at 40 (1983) (characterizing traditional state law "contract claims" and the like as those "*arising purely under State law*") (emphasis added); 130 CONG. REC. H6204-05 (daily ed. March 21, 1984) (statement of Rep. Kindness) (criticizing the original jurisdictional scheme of the 1978 Act on the ground it sought to "spread the jurisdiction of the bankruptcy court" too far, permitting bankruptcy courts to adjudicate too much, namely "*rights arising under State law*") (emphasis added); THE AMERICAN HERITAGE COLLEGE DICTIONARY 76 (4th ed. 2004) (defining words "arise" and "arising" as "4. To come into being; originate. 5. To result, issue, or proceed."); WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 117 (1986) (defining words "arise" and "arising" as "4a: to originate from a specified source...b: to come into being...6...a: to come about : come up : take place"); A DICTIONARY OF MODERN ENGLISH USAGE 35 (2d ed. 1965) (word "arise," it is said, "[i]n ordinary speech and writing...means merely to come into existence or notice or to originate *from*").

Stern (implicitly) and the Government (explicitly) contend that the Court should simply

ignore the "arising under" and "arising in" limitations in applying section 157(b). BR.26-28; USBR.18-20. Doing so, however, would be a textual disaster: not only would it render significant portions of the statute superfluous, but it also would render the statute as a whole incoherent and unconstitutional. *See Dole Food Co. v. Patrickson*, 538 U.S. 468, 476-77 (2003) ("we should not construe the statute in a manner that is strained and, at the same time, would render a statutory term superfluous").

For example, removing the "arising under" and "arising in" concepts as limitations on the broad definition of "core proceedings" would effectively gut the separate category of "related to" jurisdiction under section 157(c). Section 157(b)(2)(A) defines "core proceedings" broadly to include "matters concerning the administration of the estate." 28 U.S.C. §157(b)(2)(A). But that is also essentially the definition of "related to" proceedings: matters that "'in any way impact[] upon the handling and administration of the bankruptcy estate.'" *Celotex*, 514 U.S. at 308 n.6; *see also* Pet. App. 41-42 (discussing "related to" jurisdiction). Critically, applying the concepts of "arising under" and "arising in" prevents section 157(b)(2)(A) from overtaking section 157(c): with the "arising under" and "arising in" concepts in place, the category of "matters concerning the administration of the estate" under section 157(b)(2)(A) is properly limited to those that ei-

ther (1) constitute an administrative proceeding created by the Code, or (2) are otherwise unique to bankruptcy.

In addition, removing the "arising under" and "arising in" concepts as limitations on the broad definition of "core proceedings" would render section 157(b)(2)(O) unconstitutional. This provision defines "core proceedings" to include "proceedings affecting the liquidation of the assets of the estate." 28 U.S.C. §157(b)(2)(O). Left to its own devices, this category would subsume the adjudication of the very state law breach of contract action at issue in *Marathon*. As noted, a debtor's pre-existing cause of action is an asset that passes to the debtor's bankruptcy estate upon the bankruptcy filing. *Celotex*, 514 U.S. at 307-08 n.5; 11 U.S.C. §541. In order to liquidate such an asset, it ordinarily must be adjudicated, and any adjudication would obviously "affect" the asset's liquidation. Thus, if jurisdiction under section 157(b)(1) turns merely on whether a type of matter fits into one of the categories listed in section 157(b)(2), a bankruptcy court would be authorized under section 157(b)(2)(O) to do exactly what *Marathon* proscribes—the very result Congress intended to avoid. On the other hand, applying the "arising under" and "arising in" concepts readily prevents this from occurring by screening out such state law causes of action from the scope of section 157(b)(1) because they (1) are not created by the

Code, and (2) do not involve an administrative matter that is unique to the bankruptcy process.

The Government complains that reference to the "arising under" and "arising in" concepts as jurisdictional boundaries is undesirable because they are not defined, thereby giving little guidance to judges. USBR.19. But the same is true of the phrase "arising under" used in the general federal question jurisdictional provision, 28 U.S.C. §1331. The Government's complaint is no reason to abandon the statutory text.

The Government contends that reference to the murky provisions of section 157(b)(3) suggests that the phrases "arising under" and "arising in" have no meaning because section 157(b)(3) directs a bankruptcy judge to make the initial determination whether a particular matter is "core." USBR.18-19. This is countered, however, by the more serious problem occasioned by the Government's interpretation in connection with section 157(b)(4), which provides that "[n]on-core proceedings under section 157(b)(2)(B)...shall not be subject to the mandatory abstention provisions of section 1334(c)(2)." 28 U.S.C. §157(b)(4). Section 1334(c)(2) requires mandatory abstention for "related to" proceedings that can be timely adjudicated in a State forum. 28 U.S.C. §1334(c)(2). Under the Government's theory, there is no such thing as a "non-core" proceeding under section 157(b)(2)(B), and

thus section 157(b)(4) would have to be ignored in its entirety. In contrast, recognizing that the concepts of "arising in" and "arising under" limit the scope of "core proceedings" (effectively culling matters from the scope of section 157(b) and transferring them to the "related to" category of section 157(c)) saves section 157(b)(4) from surplusage.

The Government argues that adopting its approach would avoid a conundrum in the wording of the text owing to the fact that the section 157 does not appear to provide a jurisdictional home for items listed as "core proceedings" that do not also "arise under" or "arise in." USBR.20. This Court, however, has already suggested the answer to that concern: matters listed as examples of "core proceedings" that do not also "arise under" or "arise in" are simply to be treated as "related to" bankruptcy if they may conceivably have some impact on the administration of the estate. This follows logically and textually from the fact that there are three overarching categories of bankruptcy jurisdiction ("arising under," "arising in," and "related to") from which everything else derives. *See Celotex*, 514 U.S. at 307 (explaining that a bankruptcy court's jurisdiction "must be based on the 'arising under,' 'arising in,' or 'related to' language *of §§1334(b) and 157(a).*") (emphasis added). In any event, the Government's concerns do not justify its radical reworking of the statute.

C. Stern contends that denying bankruptcy courts the ability to decide counterclaims will "confound bankruptcy administration." BR.15. Stern is incorrect. Adherence to the commands of Article III and the governing statutory text does not mean that bankruptcy courts are barred from "hearing" all counterclaims. On the contrary, it simply limits the bankruptcy courts' ability to finally decide a narrow category of pre-existing claims that arise under state law.

Many counterclaims commonly asserted in bankruptcy "arise under" the Bankruptcy Code, such as preference actions created by section 547 of the Code and equitable subordination actions created by section 510. 11 U.S.C. §§547, 510. Likewise, many counterclaims commonly asserted in bankruptcy "arise in" a case under the Code, such as post-bankruptcy causes of action to recover property wrongfully removed from the debtor's post-bankruptcy estate. Under section 157(b)(1), the bankruptcy courts may finally decide these types of counterclaims, subject to ordinary appellate review.

In contrast, for pre-existing state law counterclaims that neither "arise under" the Code nor "arise in" a case under the Code, the bankruptcy court may still "hear" such matters (other than personal injury tort claims), but may

not finally decide them. Instead, as noted, the court enters proposed findings of fact and conclusions of law subject to plenary *de novo* review in the Article III district court. In other words, treating pre-existing state law counterclaims as "related to" matters simply alters the relevant standard of review.

Altering the standard of review does not trench seriously on bankruptcy administration. At the same time, *de novo* review preserves the essential attributes of the judicial power for the Article III tribunal. This result is both faithful to the plain meaning of Congress' jurisdictional scheme and relevant constitutional principles.

D. Stern contends that limiting the scope of section 157(b)(2)(C) (the "counterclaim" provision) would reduce it to surplusage in light of section 157(b)(2)(B) (the "allowance or disallowance of claims" provision). BR.15, 34. Stern is mistaken. Under the Bankruptcy Code, the process of allowing and disallowing claims is analytically distinct from the process of determining counterclaims in general, and state law counterclaims in particular.

As noted, section 502 of the Code does not require the adjudication of state law counterclaims in order to allow or disallow a claim. Section 502(d), however, does create an exception for certain federally created

counterclaims—*e.g*, preference actions. 11 U.S.C. §502(d) (discussing, *inter alia*, §547). By statutory directive, these must be resolved as part of the claims allowance process. Because the Bankruptcy Code creates these causes of action, however, they "arise under" the Code within the meaning of section 157(b)(1), and, under the statutory scheme, the bankruptcy court has jurisdiction to finally determine them.

It may well be, of course, that there are some state law counterclaims that are so inextricably intertwined with the creditor's claim that, as a practical matter, they must be adjudicated in order to allow or disallow the claim. If so, the bankruptcy court may hear them. But because such counterclaims do not "arise under" or "arise in," the bankruptcy court may only address them by submitting proposed findings of fact and conclusions of law (unless the parties expressly consent otherwise in writing as required by the applicable rule).

Adjusting the standard meaning of the "arising in" concept, the court below concluded that if a state-law counterclaim is so inextricably intertwined with a proof of claim that, as a practical matter, it must be adjudicated in order to determine the creditor's claim, the bankruptcy

court may finally decide it. Pet. App. 50.[14] The decision below is a plausible alternative to Elaine's argument. This Court, however, need not choose between the two because, as the court below properly concluded, Vickie's tortious interference claim is not so inextricably intertwined with Pierce's defamation claim that it had to be decided in order to allow or disallow Pierce's proof of claim. Pet. App. 51-55. Accordingly, under either approach, the decision below should be affirmed.[15]

[14] The court below reasoned that, if the concepts of "arising under" and "arising in" prevent the bankruptcy court from finally adjudicating state law counterclaims that are inextricably intertwined with a proof of claim, that would appear to create a redundancy with respect to section 157(b)(2)(C). Pet. App. 43. Section 157(b)(2)(C) includes as "core proceedings" "counterclaims by the estate against persons filing claims against the estate." The court below worried that all of the examples of counterclaims that "arise under" or "arise in" are already specifically enumerated elsewhere in section 157(b)(2) (*e.g.*, preference actions in section 157(b)(2)(F)). Pet. App. 43. The court therefore reasoned that section 157(b)(2)(C) must encompass something more. The court's concern, however, is readily redressed. Two common types of counterclaims that either "arise under" or "arise in," and are not specifically listed in section 157(b)(2), are equitable subordination actions created by section 510(c), 11 U.S.C. §510(c), and post-petition causes of action between the bankruptcy estate and others for the return of property wrongfully taken from the estate.

[15] Of course, if the Court were to conclude that, contrary to the decision below, Vickie's claim is inextricably inter-

III. The Bankruptcy Court Lacked Jurisdiction To Hear or Determine Pierce's Defamation Action Under Section 157(b)(5) and Thus Lacked Jurisdiction To Hear Vickie's "Counterclaim."

A. Federal jurisdiction cannot exist solely on the basis of a counterclaim. *See, e.g., Vaden v. Discover Bank*, 129 S. Ct. 1262, 1272 n.10 (2009) ("a counterclaim asserted in a responsive pleading cannot provide the basis for 'arising under' jurisdiction consistently with the well-pleaded complaint rule"); *Holmes Group, Inc. v. Vornado Air Circulation Sys.*, 535 U.S. 826, 830 (2002); *Caterpillar Inc. v. Williams*, 482 U.S. 386, 392 (1987). In this case, Stern contends that the Bankruptcy Court had jurisdiction to finally determine Vickie's tortious interference claim as a "counterclaim" to a claim against the estate, namely Pierce's "proof of claim for defamation," and the nexus with Pierce's claim is thus the foundation on which Stern rests his jurisdictional assertion. BR.14. The Bankruptcy Court, however, lacked jurisdiction over Pierce's

twined with Pierce's proof of claim such that, as a practical matter, the Bankruptcy Court was required to decide it in order to allow Pierce's proof of claim, Elaine submits that the "arising in" limitation on the scope of jurisdiction under section 157(b)(1) would nonetheless render her claim a "related to" matter.

defamation claim under section 157(b)(5); accordingly, it also lacked jurisdiction to resolve Vickie's "counterclaim." *Pettibone Corp. v. Easley*, 935 F.2d 120, 123 (7th Cir. 1991) (holding that bankruptcy judges cannot enter final judgments on personal injury tort claims and "[t]he whole case, including defenses of all kinds, goes off to the district court or the state court."); Pet. App. 75 (Kleinfeld, J., concurring).

Section 157(b)(5) provides that all "personal injury tort...claims shall be tried in the district court." 28 U.S.C. §157(b)(5). The wording of this statute is plain, and it unambiguously directs adjudication of personal injury tort claims in the district court, not the bankruptcy court. *See Lopez v. Davis*, 531 U.S. 230, 241 (2001) (Congress' use of the word "shall" imposes "discretionless obligations").

As explained previously, *see supra* pp. 18-20, just prior to its enactment, the Senate amended section 157 to add section 157(b)(5). As Senator Dole stated in terms as plain as the statute itself, "[o]ne of those areas reserved for attention of the district courts will be personal injury claims, which are exempted from the definition of core proceeding under the bill." 130 CONG. REC. S20083 (daily ed. June 29, 1984) (statement of Sen. Dole). As the Senator further explained, personal injury tort claims are chan-

neled away from the bankruptcy court in two ways.

First, they are channeled to the state courts through the abstention provisions of 28 U.S.C. §1334(c). 130 CONG. REC. S20083 (daily ed. June 29, 1984) (statement of Sen. Dole). ("[t]he result of the conference discussion was a provision that preserves the integrity of bankruptcy jurisdiction while allowing abstention for personal injury cases where they can be timely adjudicated in State courts.").

Second, in the absence of abstention, they are channeled to the district courts through section 157(b)(5). *Id.* ("In addition, where abstention does not occur, those cases will be handled by the district court where the bankruptcy has been filed or, if that court finds it appropriate, where the claim arose."). Thus, by statutory design, no jurisdiction to adjudicate personal injury tort claims is left in the bankruptcy courts, not even if the tort claimant files a proof of claim.

Although section 157(b)(2)(B) includes as a "core proceeding" the "allowance or disallowance of claims," it expressly *excludes* "unliquidated" (*i.e.*, unadjudicated) "personal injury tort claims." 11 U.S.C. §157(b)(2)(B). As Senator DeConcini explained, the exclusion rests on grounds of fairness: "Unlike a trade creditor who elects to do business with a particular company, the personal injury tort claimant does not choose to be

injured by a particular debtor," and therefore should not be forced to try his or her claims in bankruptcy court. 130 CONG. REC. S13076 (daily ed. May 21, 1984) (statement of Sen. DeConcini).

In this case, when Pierce filed his proof of claim, he expressly indicated that his defamation action constituted a personal injury tort. Pet. App. 78; SER-6020. Moreover, Pierce's defamation claim is properly a "personal injury tort claim" within the plain meaning of the statutory provision. *See* BLACK'S LAW DICTIONARY 802 (8th ed. 2004) (defining "personal injury" as "[a]ny invasion of a personal right, including mental suffering and false imprisonment.").

Under Texas law, a defamation action constitutes a "personal injury tort." *See In re Dillard Dep't Stores, Inc.*, 186 S.W.3d 514, 516 (Tex. 2006) ("The phrase 'personal injuries' has been interpreted by Texas courts to include injuries to reputation."). This rule is likewise the norm among the States that have considered the issue.[16] Further, numerous bankruptcy courts

[16] *See, e.g.*, N.H. Rev. Stat. Ann. §507-B:1 (2010) ("'Personal injury' means...[a]ny injury to the feelings or reputation of a natural person"); N.D. Cent. Code §32-12.2-01 (2010); *Ex parte Graham*, 634 So. 2d 994, 997 (Ala. 1993); *O'Hara v. Storer Commc'ns*, 282 Cal. Rptr. 712, 722 (Cal. Ct. App. 1991) ("defamation is a personal injury..."); *Brooks v. Jackson*, 813 P.2d 847, 848-49 (Colo. App. 1991);

have also concluded that a defamation action is a personal injury tort within the meaning of section 157(b)(5), precluding the bankruptcy court from finally resolving it. *See, e.g., In re Arnold*, 407 B.R. 849, 853 (Bankr. M.D.N.C. 2009) ("Plaintiffs' defamation claims constitute personal injury tort claims within the meaning of Section 157(b)(5)"); *In re Passialis*, 292 B.R. 346, 348 (Bankr. N.D. Ill. 2003); *Control Ctr., LLC v. Lauer*, 288 B.R. 269, 286 (M.D. Fla. 2002); *In re Goidel*, 150 B.R. 885, 888 (Bankr. S.D.N.Y. 1993).

As used in section 157(b)(5), the concept of a "personal injury tort" is not limited to bodily injury; where Congress intends to narrow "personal injury torts" to those involving bodily injury, it does so expressly. *See* 11 U.S.C. §522(d)(11) (exempting from property of the estate payments or property traceable to an award for "personal bodily injury"). Because Congress did not impose such a limitation in section

De Moss v. News-Journal Co., 408 A.2d 944, 945 (Del. 1979); *Zieve v. Hairston*, 598 S.E.2d 25, 32 (Ga. Ct. App. 2004); *New York, P. & N. R. Co. v. Waldron*, 82 A. 709, 714 (Md. 1911); *Commonwealth v. Miller*, 432 N.E.2d 463, 467 (Mass. 1982); *Small v. McRae*, 651 P.2d 982, 992 (Mont. 1982); *Gallion v. O'Connor*, 494 N.W.2d 532, 534 (Neb. 1993); *Nadra v. Mbah*, 893 N.E.2d 829, 834 (Ohio 2008); *Via v. O'Donnell*, 27 Va. Cir. 433, 445 (Va. Cir. Ct. 1982); *Hemberger v. Bitzer*, 574 N.W.2d 656, 660 (Wis. 1998).

157(b)(5), the term should be given its ordinary, intended meaning. *See Wilson v. Garcia*, 471 U.S. 261, 280 (1985) (civil rights claims brought under section 1983 "are best characterized as personal injury actions."), *superseded by statute as recognized in Jones v. R.R. Donnelley & Sons Co.*, 541 U.S. 369, 378-80 (2004). In addition, Vickie's cause of action for tortious interference with a gift is also included within the broad meaning of personal injury tort as used in section 157(b)(5). *See* JA-75 (Kleinfeld, J., concurring).

B. The Government asserts that, in considering whether the Bankruptcy Court had jurisdiction to finally decide Vickie's tortious interference counterclaim, the Court should essentially ignore section 157(b)(5). USBR.23 n.1. But "[w]ithout cross-petitioning for certiorari, a prevailing party may, of course, 'defend its judgment on any ground properly raised below whether or not that ground was relied upon, rejected, or even considered by the District Court or the Court of Appeals.'" *Granfinanciera*, 492 U.S. at 38-39. Pierce repeatedly raised section 157(b)(5) below; sought withdrawal of the reference on the basis of it; and briefed and argued it on appeal. Indeed, the concurrence below accepted it as an additional ground of decision, Pet. App. 74-76 (Kleinfeld, J., concurring), and Pierce raised it in this Court in his brief in opposition. BIO 41-43.

Moreover, the provision is jurisdictional; is subsumed within the jurisdictional questions presented; and is an integral part of the very statute at issue. Further, affirming on the basis of section 157(b)(5) avoids the constitutional issues at play in this litigation. Finally, and most important, Stern's jurisdictional theory regarding Vickie's claim unavoidably *rests* on the Bankruptcy Court's jurisdiction over Pierce's defamation claim.

Either jurisdiction to finally decide Vickie's counterclaim exists because of some compelling connection between the counterclaim and some other matter the bankruptcy court had jurisdiction to finally resolve, or the counterclaim stands entirely by itself as simply a state law claim that Vickie has against Pierce. If the former, Stern cannot prevail because the bankruptcy court had no jurisdiction to finally determine Pierce's claim. If the latter, Stern likewise cannot prevail because, if Vickie's tortious inference claim is considered independently, it lies in the same posture as the state law claim in *Marathon*. In either event, the decision below should be affirmed.

CONCLUSION

For the foregoing reasons, the decision of the court below should be affirmed.

Respectfully submitted,

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APPENDIX

APPENDIX A

Constitutional and Statutory Provisions

1. Article III, Section 1 of the United States Constitution provides:

Section 1. The judicial Power of the United States, shall be vested in one supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish. The Judges, both of the supreme and inferior Courts, shall hold their Offices during good Behaviour, and shall, at stated Times, receive for their Services, a Compensation, which shall not be diminished during their Continuance in Office.

2. 11 U.S.C. §502 provides in relevant part:

Allowance of claims or interests

(a) A claim or interest, proof of which is filed under section 501 of this title, is deemed allowed, unless a party in interest, including a creditor of a general partner in a partnership that is a debtor in a case under chapter 7 of this title, objects.

(b) Except as provided in subsections (e)(2), (f), (g), (h) and (i) of this section, if such objection to a claim is made, the court, after notice and a

hearing, shall determine the amount of such claim in lawful currency of the United States as of the date of the filing of the petition, and shall allow such claim in such amount, except to the extent that—

(1) such claim is unenforceable against the debtor and property of the debtor, under any agreement or applicable law for a reason other then because such claim is contingent or unmatured;

* * *

(d) Notwithstanding subsections (a) and (b) of this section, the court shall disallow any claim of any entity from which property is recoverable under section 542, 543, 550, or 553 of this title or that is a transferee of a transfer avoidable under section 522(f), 522(h), 544, 545, 547, 548, 549, or 724(a) of this title, unless such entity or transferee has paid the amount, or turned over any such property, for which such entity or transferee is liable under section 522(i), 542, 543, 550, or 553 of this title.

Appendix A

3. 11 U.S.C. §522(d)(11) provides in relevant part:

Exemptions

(d) The following property may be exempted under subsection (b)(2) of this section:

***

(11) The debtors right to receive, or property that is traceable to—

***

(D) a payment, not to exceed $21,625, on account of personal bodily injury, not including pain and suffering or compensation for actual pecuniary loss, of the debtor or an individual of whom the debtor is a dependent; or

4. 11 U.S.C. §541 provides in relevant part:

Property of the estate

(a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:

(1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable inter-

ests of the debtor in property as of the commencement of the case.

▲▲▲

(7) Any interest in property that the estate acquires after the commencement of the case.

5. 28 U.S.C. §152 provides in relevant part:

Appointment of bankruptcy judges

(a)(1) Each bankruptcy judge to be appointed for a judicial district, as provided in paragraph (2), shall be appointed by the court of appeals of the United States for the circuit in which such district is located. Such appointments shall be made after considering the recommendations of the Judicial Conference submitted pursuant to subsection (b). Each bankruptcy judge shall be appointed for a term of fourteen years, subject to the provisions of subsection (e). However, upon the expiration of the term, a bankruptcy judge may, with the approval of the judicial council of the circuit, continue to perform the duties of the office until the earlier of the date which is 180 days after the expiration of the term or the date of the appointment of a successor. Bankruptcy judges shall serve as judicial officers of the United States district court established under Article III of the Constitution.

6. 28 U.S.C. §153 provides in relevant part:

Salaries; character of service

(a) Each bankruptcy judge shall serve on a full-time basis and shall receive as full compensation for his services, a salary at an annual rate that is equal to 92 percent of the salary of a judge of the district court of the United States as determined pursuant to section 135, to be paid at such times as the Judicial Conference of the United States determines.

7. 28 U.S.C. §157 provides:

Procedures

(a) Each district court may provide that any or all cases under title 11 and any or all proceedings arising under title 11 or arising in or related to a case under title 11 shall be referred to the bankruptcy judges for the district.

(b)(1) Bankruptcy judges may hear and determine all cases under title 11 and all core proceedings arising under title 11, or arising in a case under title 11, referred under subsection (a) of this section, and may enter appropriate orders and judgments, subject to review under section 158 of this title.

(2) Core proceedings include, but are not limited to—

(A) matters concerning the administration of the estate;

(B) allowance or disallowance of claims against the estate or exemptions from property of the estate, and estimation of claims or interests for the purposes of confirming a plan under chapter 11, 12, or 13 of title 11 but not the liquidation or estimation of contingent or unliquidated personal injury tort or wrongful death claims against the estate for purposes of distribution in a case under title 11;

(C) counterclaims by the estate against persons filing claims against the estate;

(D) orders in respect to obtaining credit;

(E) orders to turn over property of the estate;

(F) proceedings to determine, avoid, or recover preferences;

(G) motions to terminate, annul, or modify the automatic stay;

(H) proceedings to determine, avoid, or recover fraudulent conveyances;

(I) determinations as to the dischargeability of particular debts;

(J) objections to discharges;

(K) determinations of the validity, extent, or priority of liens;

(L) confirmations of plans;

(M) orders approving the use or lease of property, including the use of cash collateral;

(N) orders approving the sale of property other than property resulting from claims brought by the estate against persons who have not filed claims against the estate;

(O) other proceedings affecting the liquidation of the assets of the estate or the adjustment of the debtor-creditor or the equity security holder relationship, except personal injury tort or wrongful death claims; and

(P) recognition of foreign proceedings and other matters under chapter 15 of title 11

(3) The bankruptcy judge shall determine, on the judge's own motion or on timely motion of a party, whether a proceeding is a core proceeding under this subsection or is a proceeding that is otherwise related to a case under title 11. A determination that a proceeding is not a core proceeding shall not be made solely on the basis that its resolution may be affected by State law.

(4) Non-core proceedings under section 157(b)(2)(B) of title 28, United States Code, shall not be subject to the mandatory abstention provisions of section 1334(c)(2).

(5) The district court shall order that personal injury tort and wrongful death claims shall be tried in the district court in which the bankruptcy case is pending, or in the district court in the district in which the claim arose, as determined by the district court in which the bankruptcy case is pending.

(c)(1) A bankruptcy judge may hear a proceeding that is not a core proceeding but that is otherwise related to a case under title 11. In such proceeding, the bankruptcy judge shall submit proposed findings of fact and conclusions of law to the district court, and any final order or judgment shall be entered by the district judge after considering the bankruptcy judge's proposed findings and conclusions and after reviewing de

novo those matters to which any party has timely and specifically objected.

(2) Notwithstanding the provisions of paragraph (1) of this subsection, the district court, with the consent of all the parties to the proceeding, may refer a proceeding related to a case under title 11 to a bankruptcy judge to hear and determine and to enter appropriate orders and judgments, subject to review under section 158 of this title.

(d) The district court may withdraw, in whole or in part, any case or proceeding referred under this section, on its own motion or on timely motion of any party, for cause shown. The district court shall, on timely motion of a party, so withdraw a proceeding if the court determines that resolution of the proceeding requires consideration of both title 11 and other laws of the United States regulating organizations or activities affecting interstate commerce.

(e) If the right to a jury trial applies in a proceeding that may be heard under this section by a bankruptcy judge, the bankruptcy judge may conduct the jury trial if specially designated to exercise such jurisdiction by the district court and with the express consent of all the parties.

8. 28 U.S.C. §158 provides in relevant part:

Appeals

(a) The district courts of the United States shall have jurisdiction to hear appeals

(1) from final judgments, orders, and decrees;

(2) from interlocutory orders and decrees issued under section 1121(d) of title 11 increasing or reducing the time periods referred to in section 1121 of such title; and

(3) with leave of the court, from other interlocutory orders and decrees;

and, with leave of the court, from interlocutory orders and decrees, of bankruptcy judges entered in cases and proceedings referred to the bankruptcy judges under section 157 of this title. An appeal under this subsection shall be taken only to the district court for the judicial district in which the bankruptcy judge is serving.

9. 28 U.S.C. §1334 provides:

Bankruptcy cases and proceedings

(a) Except as provided in subsection (b) of this section, the district courts shall have original and exclusive jurisdiction of all cases under title 11.

(b) Except as provided in subsection (e)(2), and notwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the district courts, the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11.

(c)(1) Except with respect to a case under chapter 15 of title 11, nothing in this section prevents a district court in the interest of justice, or in the interest of comity with State courts or respect for State law, from abstaining from hearing a particular proceeding arising under title 11 or arising in or related to a case under title 11.

(2) Upon timely motion of a party in a proceeding based upon a State law claim or State law cause of action, related to a case under title 11 but not arising under title 11 or arising in a case under title 11, with respect to which an action could not have been commenced in a court of the

United States absent jurisdiction under this section, the district court shall abstain from hearing such proceeding if an action is commenced, and can be timely adjudicated, in a State forum of appropriate jurisdiction.

(d) Any decision to abstain or not to abstain made under subsection (c) (other than a decision not to abstain in a proceeding described in subsection (c)(2)) is not reviewable by appeal or otherwise by the court of appeals under section 158(d), 1291, or 1292 of this title or by the Supreme Court of the United States under section 1254 of this title. Subsection (c) and this subsection shall not be construed to limit the applicability of the stay provided for by section 362 of title 11, United States Code, as such section applies to an action affecting the property of the estate in bankruptcy.

(e) The district court in which a case under title 11 is commenced or is pending shall have exclusive jurisdiction--

(1) of all the property, wherever located, of the debtor as of the commencement of such case, and of property of the estate; and

(2) over all claims or causes of action that involve construction of section 327 of title 11, United States Code, or rules relating to disclo-

sure requirements under section 327.

10. Act of July 1, 1898, ch. 541, 30 Stat. 544 (repealed 1979) provides in relevant part:

CHAPTER II.

CREATION OF COURTS OF BANKRUPCY AND THEIR JURISDICTION.

SEC. 2. That the courts of bankruptcy as hereinbefore defined, viz, the district courts of the United States in the several States, the supreme court of the District of Columbia, the district courts of the several Territories, and the United States courts in the Indian Territory and the District of Alaska, are hereby made courts of bankruptcy, and are hereby invested, within their respective territorial limits as now established, or as they may be hereafter changed, with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in bankruptcy proceedings, in vacation in chambers and during their respective terms, as they are now or may be hereafter held, to (1) adjudge persons bankrupt who have had their principal place of business, resided, or had their domicile within their respective territorial jurisdictions for the preceding six months, or the greater portion thereof, or who do not have their principal place of business, reside, or have their domicile

within the United States, but have property within their jurisdictions, or who have been adjudged bankrupts by courts of competent jurisdiction without the United States and have property within their jurisdictions; (2) allow claims, disallow claims, reconsider allowed or disallowed claims, and allow or disallow them against bankrupt estates; (3) appoint receivers or the marshals, upon application of parties in interest, in case the courts shall find it absolutely necessary, for the preservation of estates, to take charge of the property of bankrupts after the filing of the petition and until it is dismissed or the trustee is qualified; (4) arraign, try, and punish bankrupts, officers, and other persons, and the agents, officers, members of the board of directors or trustees, or other similar controlling bodies, of corporations for violations of this Act, in accordance with the laws of procedure of the United States now in force, or such as may be hereafter enacted, regulating trials for the alleged violation of laws of the United States; (5) authorize the business of bankrupts to be conducted for limited periods by receivers, the marshals, or trustees, if necessary in the best interests of the estates; (6) bring in and substitute additional persons or parties in proceedings in bankruptcy when necessary for the complete determination of a matter in controversy; (7) cause the estates of bankrupts to be collected, reduced to money and distributed, and determine contro-

versies in relation thereto, except as herein otherwise provided; (8) close estates, whenever it appears that they have been fully administered, by approving the final accounts and discharging the trustees, and reopen them whenever it appears they were closed before being fully administered; (9) confirm or reject compositions between debtors and their creditors, and set aside compositions and reinstate the cases; (10) consider and confirm, modify or overrule, or return, with instructions for further proceedings, records and findings certified to them by referees; (11) determine all claims of bankrupts to their exemptions; (12) discharge or refuse to discharge bankrupts and set aside discharges and reinstate the cases; (13) enforce obedience by bankrupts, officers, and other persons to all lawful orders, by fine or imprisonment or fine and imprisonment; (14) extradite bankrupts from their respective districts to other districts; (15) make such orders, issue such process, and enter such judgments in addition to those specifically provided for as may be necessary for the enforcement of the provisions of this Act; (16) punish persons for contempts committed before referees; (17) pursuant to the recommendation of creditors, or when they neglect to recommend the appointment of trustees, appoint trustees, and upon complaints of creditors, remove trustees for cause upon hearings and after notices to them; (18) tax costs, whenever they are allowed by law,

and render judgments therefor against the unsuccessful party, or the successful party for cause, or in part against each of the parties, and against estates, in proceedings in bankruptcy; and (19) transfer cases to other courts of bankruptcy.

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CHAPTER V.

OFFICERS, THEIR DUTIES AND COMPENSATION.

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SEC. 38. JURISDICTION OF REFEREES.—a. Referees respectively are hereby invested, subject always to a review by the judge, within the limits of their districts as established from time to time, with jurisdiction to (1) consider all petitions referred to them by the clerks and make the adjudications or dismiss the petitions; (2) exercise the powers vested in courts of bankruptcy for the administering of oaths to and the examination of persons as witnesses and for requiring the production of documents in proceedings before them, except the power of commitment; (3) exercise the powers of the judge for the taking possession and releasing of the property of the bankrupt in the event of the issuance by the clerk of a certificate showing the absence of a judge from the judicial district, or the division of the district, or his sickness, or inability to act; (4) perform such part of the duties, except as to

questions arising out of the applications of bankrupts for compositions or discharges, as are by this Act conferred on courts of bankruptcy and as shall be prescribed by rules or orders of the courts of bankruptcy of their respective districts, except as herein otherwise provided; and (5) upon the application of the trustee during the examination of the bankrupts, or other proceedings, authorize the employment of stenographers at the expense of the estates at a compensation not to exceed ten cents per folio for reporting and transcribing the proceedings.

11. Act of July 1, 1898, ch. 541, 30 Stat. 544, *as amended by* Act of May 27, 1926, ch. 406, 44 Stat. 662, 664 (repealed 1979) provides in relevant part:

CHAPTER IV.

COURTS AND PROCEDURE THEREIN.

* * *

SEC. 23. JURISDICTION OF UNITED STATES AND STATE COURTS.—a. The United States district courts shall have jurisdiction of all controversies at law and in equity, as distinguished from proceedings in bankruptcy, between trustees as such and adverse claimants concerning the property acquired or claimed by the trustees, in the same manner and to the same extent only as though bankruptcy proceedings had not been in-

stituted and such controversies had been between the bankrupts and such adverse claimants.

b. Suits by the trustee shall be brought or prosecuted only in the courts where the bankrupt, whose estate is being administered by such trustee, might have brought or prosecuted them if proceedings in bankruptcy had not been instituted, unless by consent of the proposed defendant, except suits for the recovery of property under section 60, subdivision b; section 67, subdivision e; and section 70, subdivision e.

APPENDIX B
Proposed Bills

1. H.R. 6978, 97th Cong. (2d Sess. 1982), as proposed on August 12, 1982, provides in relevant part:

SEC. 33. (a) Title 28 of the United States Code is amended by inserting after chapter 89 the following new chapter:

"CHAPTER 90—BANKRUPTCY COURTS

***

"§ 1471. Jurisdiction.

"(a) Except as provided in subsection (b) of this section, the bankruptcy courts shall have original and exclusive jurisdiction of all cases under title 11.

"(b) Notwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the bankruptcy courts, the bankruptcy courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11 or arising in or related to cases under title 11.

"(c) Subsection (b) of this section does not prevent a bankruptcy court, in the interest of justice, from abstaining from hearing a particular proceeding arising under title 11 or arising in or related to a case under title 11. Such abstention,

or a decision not to abstain, is not reviewable by appeal or otherwise.

"(d) The bankruptcy court in which a case under title 11 is pending shall have exclusive jurisdiction of all of the property, wherever located, of the debtor, as of the commencement of the case.

***

"§ 1481. Powers of bankruptcy court

"A bankruptcy court shall have the powers of a court of equity, law, and admiralty.

"§ 1482. Appeals

"(a) Bankruptcy appellate panels established in section 159(a) of this title shall have jurisdiction of appeals from all final judgments, orders, and decrees of bankruptcy courts.

"(b) Bankruptcy appellate panels shall have jurisdiction of appeals from interlocutory judgments, orders, and decrees of bankruptcy courts, but only by leave of the panel to which the appeal is taken."

2. S. 1013, 98th Cong. (1st Sess. 1983), as referred to the House Committee on the Judiciary on May 4, 1983, provides in relevant part:

Sec. 102. (a) Title 28, United States Code, is amended by inserting after chapter 89 the following:

"CHAPTER 90—DISTRICT COURTS AND BANKRUPTCY COURTS

* * *

"§ 1471. Jurisdiction

"(a) Except as provided in subsection (b) of this section, the district courts shall have original and exclusive jurisdiction of all cases under title 11.

"(b) Notwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the district courts, the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11.

"(c) All cases under title 11 and all civil proceedings arising under title 11, or arising in or related to cases under title 11 shall be referred to the bankruptcy court for the district. The bankruptcy court for the district in which a case or proceeding under title 11 is pending shall have the authority to exercise all of the jurisdiction conferred on the district courts by subsections (a)

and (b) of this section, except where inconsistent with the Constitution, unless such case or proceeding has been recalled by the district court.

"(d) The district court on its own motion may recall any case or proceeding referred to the bankruptcy court under subsection (c) of this section.

"(e)(1) Any party, or the bankruptcy judge, may file a petition for recall of any civil case or proceeding referred to the bankruptcy court under subsection (c). Such petition shall be filed with the clerk of the district court for the district, and shall contain a short and plain statement of the grounds for recall. Written notice of the filing of such a petition shall be given promptly to all parties.

"(2) Recall of a proceeding pursuant to such petition may be granted in the discretion of the district court, except that recall shall be granted—

> "(A) with respect to a proceeding involving a claim or cause of action which is not one arising under title 11; or
>
> "(B) where the district court determines that resolution of the proceeding requires consideration of both title 11 and other laws of the United States regulating organizations or activities affecting interstate commerce.

"(f) A case or proceeding which has been recalled by the district court under this section shall be determined by the district court. The court, in its discretion, may determine the entire case. In any case or proceeding before the district court pursuant to subsection (d) or (e), such court may—

"(1) designate any bankruptcy judge within the district to serve as a special master to hear such case or proceeding and to make findings and recommendations pursuant to the Federal Rules of Civil Procedure, notwithstanding Rule 53(b) thereof, or

"(2) refer such case or proceeding to a United States magistrate in accordance with the provisions of section 636 of this title as applicable to civil proceedings generally, or to a bankruptcy judge, who shall exercise all of the jurisdiction and powers of a United States magistrate under section 636.

For purposes of this section, the district court shall use the standard of review provided in Rule 53(e)(2) of the Federal Rules of Civil Procedure or section 636(b) of this title, as the case may be, unless the court, in its designation of the special master or its referral to the magistrate orders otherwise.

"(g) Notwithstanding the provisions of subsection (e), and subject to a right to appeal pursuant to section 1334 of this title, any party to a case or

proceeding under subsection (a) or (b) of this section shall be deemed to have consented to the exercise of jurisdiction by the bankruptcy court to determine the entire matter if the party has failed to file a timely petition pursuant to subsection (e)(1) of this section. Such a petition must be filed together with the initial pleading of the party.

"(h)(1) Nothing in this section prevents a district court in the interest of justice, or in the interest of comity with State courts and respect for State law, from abstaining from hearing a particular proceeding arising under title 11 or arising in or related to a case under title 11. Such abstention, or a decision not to abstain, is not reviewable by appeal or otherwise.

"(2) In the case of a proceeding involving the debtor which is based upon a claim or cause of action arising under State law, the Court shall, upon proper motion, abstain from adjudicating such claim in the bankruptcy proceeding where an action to adjudicate such claim has been or will be instituted and timely prosecuted in a State forum of appropriate jurisdiction: *Provided*, That this paragraph shall not be construed to otherwise limit the applicability of the stay provided for by section 362 of title 11, United States Code, as such section governs an action affecting the property of the estate in bankruptcy.

"(3) A motion to abstain pursuant to this subsection shall be filed within ten days of the granting of a petition to recall pursuant to subsection 1741(e).

"(i) Subject to the provisions of this section, the bankruptcy court in which a case, under title 11 is commenced or pending may exercise jurisdiction over all property, wherever located, of the debtor or the estate as of the date of the commencement of such case.

3. H.R. 5174, 98th Cong. (2d Sess. 1984), as introduced on March 19, 1984, provides in relevant part:

SEC. 132. (a) Title 28 of the United States Code is amended by inserting after chapter 89 the following new chapter:

"CHAPTER 90—BANKRUPTCY COURTS

* * *

"§1471. Jurisdiction

"(a) Except as provided in subsection (b) of this section, the bankruptcy courts shall have original and exclusive jurisdiction of all cases under title 11.

"(b) Notwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the bankruptcy courts, the bank-

ruptcy courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11 or arising in or related to cases under title 11.

"(c) Subsection (b) of this section does not prevent a bankruptcy court, in the interest of justice, from abstaining from hearing a particular proceeding arising under title 11 or arising in or related to a case under title 11. Such abstention, or a decision not to abstain, is not reviewable by appeal or otherwise.

"(d) The bankruptcy court in which a case under title 11 is pending shall have exclusive jurisdiction of all of the property, wherever located, of the debtor, as of the commencement of the case.

* * *

"§ 1481. Powers of bankruptcy court

"A bankruptcy court shall have the powers of a court of equity, law, and admiralty.

"§ 1482. Appeals

"(a) Bankruptcy appellate panels established in section 159(a) of this title shall have jurisdiction of appeals from all final judgments, orders, and decrees of bankruptcy courts.

"(b) Bankruptcy appellate panels shall have jurisdiction of appeals from interlocutory judgments, orders, and decrees of bankruptcy courts,

but only by leave of the panel to which the appeal is taken."

4. H.R. 5174, 98th Cong. (2d Sess. 1984), as enacted by the House and referred to the Senate on March 22, 1984, provides in relevant part:

TITLE I—BANKRUPTCY JURISDICTION AND PROCEDURE

SEC. 101. (a) Section 1334 of title 28, United States Code, is amended to read as follows:

"(a) Except as provided in subsection (b) of this section, the district courts shall have original and exclusive jurisdiction of all cases under title 11.

"(b) Notwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the district courts, the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11 or arising in or related to cases under title 11.

"(c) Nothing in this section prevents a district court in the interest of justice or in the interest of comity with State courts and respect for State law, from abstaining from hearing a particular proceeding arising in or related to a case under title 11. Upon the timely motion of a party in a proceeding based upon a State law claim or State

law cause of action, related to a case under title 11 but not arising under title 11 or arising in a case under title 11, with respect to which an action could not have been commenced in a court of the United States absent jurisdiction under this section, the district court shall abstain from hearing such proceeding if an action is commenced, and can be timely adjudicated, in a State forum of appropriate jurisdiction. Any decision to abstain made under this subsection is not reviewable by appeal or otherwise. This subsection shall not be construed to limit the applicability of the stay provided for by section 362 of title 11, United States Code, as such section applies to an action affecting the property of the estate in bankruptcy.

"(d) The district court in which a case under title 11 is commenced or is pending shall have jurisdiction of all of the property, wherever located, of the debtor, as of the commencement of such case, and of all of the property of the estate.".

(b) The heading for section 1334 of title 28, United States Code, is amended to read as follows:

"§ 1334. Bankruptcy cases and proceedings".

(c) The table of sections of chapter 85 of title 28, United States Code, is amended by amending the item relating to section 1334 to read as follows:

"§ 1334. Bankruptcy cases and proceedings".

***

SEC. 104. (a) Title 28 of the United States Code is amended by inserting after chapter 5 the following new chapter:

"CHAPTER 6—BANKRUPTCY JUDGES

***

"§ 157. Procedures

"(a) Each district court may provide that any or all cases under title 11 and any or all proceedings arising under title 11 or arising in or related to a case under title 11 shall be referred to the bankruptcy judges for the district.

"(b)(l) Bankruptcy judges may hear and determine all cases under title 11 and all core proceedings arising under title 11, or arising in a case under title 11, referred under subsection (a) of this section, and may enter appropriate orders and judgments, subject to review under section 158 of this title.

"(2) Core proceedings include, but are not limited to:

"(A) matters concerning the administration of the estate;

"(B) allowance or disallowance of claims against the estate or exemptions from property of the estate;

"(C) counterclaims by the estate against persons filing claims against the estate;

"(D) orders in respect to obtaining credit;

"(E) orders to turn over property of the estate;

"(F) proceedings to determine or set aside preferences;

"(G) motions to lift or modify the automatic stay;

"(H) proceedings to set aside fraudulent conveyances;

"(I) determinations as to the dischargeability of particular debts;

"(J) objections to discharges;

"(K) determinations of the validity, extent, or priority of liens;

"(L) confirmations of plans;

"(M) orders approving the sale of property not resulting from claims brought by the estate against persons who have not filed claims against the estate; and

"(N) other proceedings affecting the liquidation of the assets of the estate or the adjust-

ment of the debtor-creditor or the equity security holder relationship.

"(3) The bankruptcy judge may determine, on the judge's own motion or on timely motion of a party, whether a proceeding is a core proceeding under this subsection or is a proceeding that is otherwise related to a case under title 11. A determination that a proceeding is not a core proceeding shall not be made solely on the basis that its resolution may be affected by state law.

"(c)(1) A bankruptcy judge may hear a proceeding that is not a core proceeding but that is otherwise related to a case under title 11. In such proceeding, the bankruptcy judge shall submit proposed findings of fact and conclusions of law to the district court, and any final order or judgment shall be entered by district judge after considering the bankruptcy judge's proposed findings and conclusions and after reviewing de novo those matters to which any party has timely and specifically objected.

"(2) Notwithstanding the provisions of paragraph (1) of this subsection, the district court, with the consent of all the parties to the proceeding, may refer a proceeding related to a case under title 11 to a bankruptcy judge to hear and determine and to enter appropriate orders and judgments, subject to review under section 158 of this title.

"(d) The district court may withdraw, in whole or in part, any case or proceeding referred under this section, on its own motion or on timely motion of any party, for cause shown. The district court shall, on timely motion of a party, so withdraw a proceeding if the court determines that resolution of the proceeding requires consideration of both title 11 and other laws of the United States regulating organizations or activities affecting interstate commerce.

"§ 158. Appeals

"(a) The district courts of the United States shall have jurisdiction to hear appeals from final judgments, orders, and decrees, and from interlocutory orders and decrees, of bankruptcy judges entered in cases and proceedings referred to the bankruptcy judges under section 157 of this title. And appeal under this subsection shall be taken only to the district court for the judicial district in which the bankruptcy judge is serving.

"(b) An appeal to a district court under subsection (a) of this section shall be taken in the same manner as appeals in civil proceedings generally are taken to the courts of appeals from the district courts.

"(c) The courts of appeals shall have jurisdiction of appeals from all final decisions, judgments, orders, and decrees of the district courts entered under this section."

5. Amendment No. 3083 to H.R. 5174, 98th Cong. (2d Sess. 1984), as proposed by Senator Thurmond on May 21, 1984 (130 CONG. REC. S13086 (daily ed. May 21, 1984)), provides in relevant part:

TITLE I—BANKRUPTCY JURISDICTION AND PROCEDURE

SEC. 101. (a) Section 1334 of title 28. United States Code, is amended to read as follows:

"§ 1334. Bankruptcy cases and proceedings

"(a) Except as provided in subsection (b) of this section, the district courts shall have original and exclusive jurisdiction of all cases under title 11.

"(b) Notwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the district courts, the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11.

"(c)(1) Nothing in this section prevents a district court in the interest of justice, or in the interest of comity with State courts or respect for State law, from abstaining from hearing a par-

ticular proceeding arising under title 11 or arising in or related to a case under title 11. Such decision to abstain or to not abstain is not reviewable by appeal or otherwise.

"(2) In a proceeding involving the debtor which is based upon a State law claim or cause of action neither arising under title 11 nor arising in a case under title 11, which could not otherwise have been brought in Federal court absent jurisdiction under this section, the court shall, upon proper motion, abstain from adjudicating such claim in the bankruptcy proceeding where an action to adjudicate such claim has been or will be timely instituted and prosecuted in a State forum of appropriate jurisdiction: *Provided*, that this paragraph shall be construed to limit the applicability of the stay provided for by section 362 of title 11, United States Code, only to the extent necessary to permit adjudication but not the execution of such claim by the State forum. Such abstention is not reviewable by appeal or otherwise.

"(3) A motion to abstain pursuant to this subsection shall be filed with the initial pleading.

"(d) The district court in which a case under title 11 is commenced or is pending shall have exclusive jurisdiction of all of the property, wher-

ever located, of the debtor, or of the estate, as of the commencement of such case.

(b) The table of sections for chapter 85 of title 28, United States Code, is amended by amending the item relating to section 1334 to read as follows:

"1334. Bankruptcy cases and proceedings.".

***

"§ 157. Procedures

"(a) Each district court may provide that any or all cases under title 11 and any or all proceedings arising under title 11 or arising in or related to a case under title 11 shall be referred to the bankruptcy judges for the district.

"(b)(1) Bankruptcy judges may hear and determine all cases under title 11 and all core proceedings arising under title 11, or arising in a case under title 11, referred under subsection (a) of this section, and may enter appropriate orders and judgments, subject to review under section 158 of this title.

"(2) Core proceedings include, but are not limited to-

"(A) matters concerning the administration of the estate;

"(B) allowance or disallowance of claims against the estate or exemptions from property of the estate, but not the liquidation or estimation of contingent or unliquidated claims against the estate;

"(C) counterclaims by the estate against persons filing claims against the estate;

"(D) orders in respect to obtaining credit;

"(E) orders to turn over property of the estate;

"(E) orders to turn over property of the estate;

"(F) proceedings to determine or set aside preferences;

"(H) proceedings to set aside fraudulent conveyances;

"(I) determinations as to the dischargeability of particular debts;

"(J) objections to discharges;

"(K) determinations of the validity, extent, or priority of liens;

"(L) confirmations of plans; and

"(M) orders approving the sale of property not resulting from claims brought by the estate against persons who have not filed claims against the estate.

"(3) The bankruptcy judge shall determine, on the judge's own motion or on timely motion of a party, whether a proceeding is a core proceeding under this subsection or is a proceeding that is otherwise related to a case under title 11. A determination that a proceeding is not a core proceeding shall not be made solely on the basis that its resolution may be affected by State law.

"(c)(1) a bankruptcy judge may hear a proceeding that is not a core proceeding but that is otherwise related to a case under title 11. In such proceeding, the bankruptcy judge shall submit proposed findings of fact and conclusions of law to the district court, and any final order or judgment shall be entered by the district judge after considering the bankruptcy judge's proposed findings and conclusions and after reviewing de novo those matters to which any party has timely and specifically objected.

"(2) Notwithstanding the provisions of paragraph (1) of this subsection, the district court, with the consent of all the parties to the proceed-

ing, may refer a proceeding related to a case under title 11 to a bankruptcy judge to hear and determine and to enter appropriate orders and judgments, subject to review under section 158 of this title.

"(d) The district court may withdraw, in whole or in part, any case or proceeding referred under this section, on its own motion or on timely motion of any party, for cause shown. The district court shall, on timely motion of a party, so withdraw a proceeding if the court determines that resolution of the proceeding requires consideration of both title 11 and other laws of the United States regulating organizations or activities affecting interstate commerce.

"§ 158. Appeals

"(a) The district courts of the United States shall have jurisdiction to hear appeals from final judgments, orders, and decrees, and, with leave of the court, from interlocutory orders and decrees, of bankruptcy judges entered in cases and proceedings referred to the bankruptcy judges under section 157 of this title. An appeal under this subsection shall be taken only to the district court for the judicial district in which the bankruptcy judge is serving.

"(b)(1) The judicial council of a circuit may establish a bankruptcy appellate panel, comprised of bankruptcy judges from districts within the circuit, to hear and determine, upon the consent of all the parties, appeals under subsection (a) of this section.

"(2) No appeal may be referred to a panel under this subsection unless the district judges for the district, by majority vote, authorize such referral of appeals originating within the district.

"(3) A bankruptcy judge may not hear an appeal originating within a district for which the judge is appointed or designated under section 152 of this title.

"(c) An appeal to a district court under subsections (a) and (b) of this section shall be taken in the same manner as appeals in civil proceedings generally are taken to the courts of appeals from the district courts.

"(d) The courts of appeals shall have jurisdiction of appeals from all final decisions, judgments, orders, and decrees of the district courts entered under subsections (a) and (b) of this section."

6. Amendment No. 3087 to Amendment No. 3083 proposed by Senator Thurmond, as proposed by Senator DeConcini on May 21, 1984 (130 CONG. REC. S13107 (daily ed. May 21, 1984)), provides in relevant part:

TITLE I—BANKRUPTCY JURISDICTION AND PROCEDURE

SEC. 101. (a) Section 1334 of title 28, United States Code, is amended to read as follows:

"§ 1134. Bankruptcy cases and proceedings

"(a) Except as provided in subsection (b) of this section, the district courts shall have original and exclusive jurisdiction of all cases under title 11.

"(b) Notwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the district courts, the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11.

"(c)(1) Nothing in this section prevents a district court in the interest of justice, or in the interest of comity with State courts or respect for State law from abstaining from hearing a particular proceeding arising under title 11 or aris-

ing in or related to a case under title 11. Such decision to abstain or to not abstain is not reviewable by appeal or otherwise.

"(2) "In a proceeding brought by the trustee which is based upon a State law claim or cause of action neither arising under title 11 nor arising in a case under title 11, which could not otherwise have been brought in Federal court absent jurisdiction under this section, the court shall upon timely motion of the party against whom the claim is brought, abstain from adjudicating such claim in the bankruptcy proceeding where (1) such claim will be timely adjudicated in a State forum of appropriate jurisdiction and (2) abstention would not be detrimental to the best interests of the estate. Such abstention is not reviewable by appeal or otherwise."

"(3) A motion to abstain pursuant to this subsection shall be filed with the initial appearance of the party.

"(d) The district court in which a case under title 11 is commenced or is pending shall have exclusive jurisdiction of all of the property, wherever located, of the debtor, as of the commencement of such case, and the estate.".

(b) The table of sections for chapter 85 of title 28, United States Code, is amended by amending

the item relating to section 1334 to read as follows:

"1334. Bankruptcy cases and proceedings.".

***

"§ 157. Procedures

"(a) Each district court may provide that any or all cases under title 11 and any or all proceedings arising under title 11 or arising in or related to a case under title 11 shall be referred to the bankruptcy judges for the district.

"(b)(1) Bankruptcy judges may hear and determine all cases under title 11 and all core proceedings arising under title 11, or arising in a case under title 11, referred under subsection (a) of this section, and may enter appropriate orders and judgments, subject to review under section 158 of this title.

"(2) Core proceedings include, but are not limited to—

"(A) matters concerning the administration of the estate;

"(B) allowance or disallowance of claims against the estate or exemptions from property of the estate, but not the liquidation or estima-

tion of contingent or unliquidated personal injury tort claims against the estate;

"(C) counterclaims by the estate against persons filing claims against the estate;

"(D) orders in respect to obtaining credit;

"(E) orders to turn over property of the estate;

"(F) proceedings to determine, avoid, or recover preferences;

"(G) motions to terminate, annul, or modify the automatic stay;

"(H) proceedings to determine, avoid, or recover fraudulent conveyances;

"(I) determinations as to the dischargeability of particular debts;

"(J) objections to discharges;

"(K) determinations of the validity, extent, or priority of liens;

"(L) confirmations of plans;

"(M) orders approving the use or lease of property, including the use of cash collateral; and

"(N) orders approving the sale of property other than property resulting from claims brought by the estate against persons who have not filed claims against the estate.

"(3) The bankruptcy judge shall determine, on the judge's own motion or on timely motion of a party, whether a proceeding is a core proceeding under this subsection or is a proceeding that is otherwise related to a case under title 11. A determination that a proceeding is not a core proceeding shall not be made solely on the basis that its resolution may be affected by State law. A motion by a party under this section shall be filed with the initial appearance of the party in the proceeding.

"(c)(1) A bankruptcy judge may hear a proceeding that is not a core proceeding but that is otherwise related to a case under title 11. In such proceeding, the bankruptcy judge shall submit proposed findings of fact and conclusions of law to the district court, and any final order or judgment shall be entered by the district judge after considering the bankruptcy judge's proposed findings and conclusions and after review-

ing de novo those matters to which any party has timely and specifically objected.

"(2) Notwithstanding the provisions of paragraph (1) of this subsection, the district court, with the consent of all the parties to the proceeding, may refer a proceeding related to a case under title 11 to a bankruptcy judge to hear and determine and to enter appropriate orders and judgments, subject to review under section 158 of this title. In any such proceeding the debtor, trustee, creditors committee, representation of the estate and examiner shall be deemed to have consented to have the proceeding referred to the bankruptcy court.

"(d) The district court may withdraw, in whole or in part, any case or proceeding referred under this section, on its own motion or on timely motion of any party, for cause shown. The district court shall, on timely motion of a party, so withdraw a proceeding if the court determines that resolution of the proceeding requires consideration of both title 11 and other laws of the United States regulating organizations or activities affecting interstate commerce. Any such motion of a party shall be filed with the initial appearance of the party in the proceeding.

"§ 158. Appeals

"(a) The district courts of the United States shall have jurisdiction to hear appeals from fiscal judgments, orders, and decrees and, with leave of the court, from interlocutory orders and decrees, of bankruptcy judges entered in cases and proceedings referred to the bankruptcy judges under section 157 of this title. An appeal under this subsection shall be taken only to the district court for the judicial district in which the bankruptcy judge is serving.

"(d)(1) The judicial council of a circuit may establish a bankruptcy appellate panel, comprised of bankruptcy judges from districts within the circuit, to hear and determine, upon the consent of all the parties, appeals under subsection (a) of this section.

"(2) No appeal may be referred to a panel under this subsection unless the district judges for the district, by majority vote, authorize such referral of appeals originating within the district.

"(3) A panel established under this section shall consist of three bankruptcy judges, provided a bankruptcy judge may not hear an appeal originating within a district for which the judge is appointed or designated under section 152 of this title.

"(c) An appeal under subsections (a) and (b) of this section shall be taken in the same manner as appeals in civil proceedings generally are taken to the courts of appeals from the district courts and in the time provided by Rule 8002 of the Bankruptcy Rules.

"(d) The courts of appeals shall have jurisdiction of appeals from all final decisions, judgments, orders, and decrees entered under subsections (a) and (b) of this section.".

(b) The table of chapters of part I of title 28, United States Code, is amended by inserting after the item relating to chapter 5, the following new item:

"6. Bankruptcy judges..... 151.".

7. H.R. 5174, 98th Cong. (2d Sess. 1984), as reported from the committee of conference on June 29, 1984 (130 CONG. REC. H20206 (daily ed. June 29, 1984)), provides in relevant part:

TITLE I—BANKRUPTCY JURISDICTION AND PROCEDURE

SEC. 101. (a) Section 1334 of title 28, United States Code, is amended to read as follows:

"§ 1334. Bankruptcy cases and proceedings

"(a) Except as provided in subsection (b) of this section, the district courts shall have original and exclusive jurisdiction of all cases under title 11.

"(b) Notwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the district courts, the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11.

"(c)(1) Nothing in this section prevents a district court in the interest of justice, or in the interest of comity with State courts or respect for State law, from abstaining from hearing a particular proceeding arising under title 11 or arising in or related to a case under title 11.

"(2) Upon timely motion of a party in a proceeding based upon a State law claim or State law cause of action, related to a case under title 11 but not arising under title 11 or arising in a case under title 11, with respect to which an action could not have been commenced in a court of the United States absent jurisdiction under this section, the district court shall abstain from hearing such proceeding if an action is commenced, and can be timely adjudicated, in a State forum of appropriate jurisdiction. Any decision to abstain made under this subsection is not reviewable by appeal or otherwise. This subsection shall not be construed to limit the applicability of the stay provided for by section 362 of title 11, United States Code, as such section applies to an action affecting the property of the estate in bankruptcy.

"(d) The district court in which a case under title 11 is commenced or is pending shall have exclusive jurisdiction of all of the property, wherever located, of the debtor as of the commencement of such case, and of the estate.".

(b) The table of sections for chapter 85 of title 28, United States Code, is amended by amending the item relating to section 1334 to read as follows:

"1334. Bankruptcy cases and proceedings.".

***

"§ 157. Procedures

"(a) Each district court may provide that any or all cases under title 11 and any or all proceedings arising under title 11 or arising in or related to a case under title 11 shall be referred to the bankruptcy judges for the district.

"(b)(1) Bankruptcy judges may hear and determine all cases under title 11 and all core proceedings arising under title 11, or arising in a case under title 11, referred under subsection (a) of this section, and may enter appropriate orders and judgments, subject to review under section 158 of this title.

"(2) Core proceedings include, but are not limited to—

"(A) matters concerning the administration of the estate;

"(B) allowance or disallowance of claims against the estate or exemptions from property of the estate, and estimation of claims or interest for the purposes of confirming a plan under chapter 11 or 13 of title 11 but not the liquidation or estimation of contingent or unliquidated personal injury tort or wrongful death claims

against the estate for purposes of distribution in a case under title 11;

"(C) counterclaims by the estate against persons filing claims against the estate;

"(D) orders in respect to obtaining credit;

"(E) orders to turn over property of the estate;

"(F) proceedings to determine, avoid, or recover preferences;

"(G) motions to terminate, annul or modify the automatic stay;

"(H) proceedings to determine, avoid, or recover fraudulent conveyances;

"(I) determinations as to the dischargeability of particular debts;

"(J) objections to discharges;

"(K) determinations of the validity, extent, or priority of liens;

"(L) confirmations of plans;

"(M) orders approving the use or lease of property, including the use of cash collateral;

"(N) orders approving the sale of property other than property resulting from claims brought by the estate against persons who have not filed claims against the estate; and

"(O) other proceedings affecting the liquidation of the assets of the estate or the adjustment of the debtor-creditor or the equity security holder relationship, except personal injury tort or wrongful death claims.

"(3) The bankruptcy judge shall determine, on the judge's own motion or on timely motion of a party, whether a proceeding is a core proceeding under this subsection or is a proceeding that is otherwise related to a case under title 11. A determination that a proceeding is not a core proceeding shall not be made solely on the basis that its resolution may be affected by State law.

"(4) Non-core proceedings under section 157(b)(2)(B) of title 28, United States Code, shall not be subject to the mandatory abstention provisions of section 1334(c)(2).

"(5) The district court shall order that personal injury tort and wrongful death claims shall be tried in the district court in which the bank-

ruptcy case is pending, or in the district court in the district in which the claim arose, as determined by the district court in which the bankruptcy case is pending.

"(c)(1) A bankruptcy judge may hear a proceeding that is not a core proceeding but that is otherwise related to a case under title 11. In such proceeding, the bankruptcy judge shall submit proposed findings of fact and conclusions of law to the district court, and any final order or judgment shall be entered by the district judge after considering the bankruptcy judge's proposed findings and conclusions and after reviewing de novo those matters to which any party has timely and specifically objected.

"(2) Notwithstanding the provisions of paragraph (1) of this subsection, the district court, with the consent of all the parties to the proceeding, may refer a proceeding related to a case under title 11 to a bankruptcy judge to hear and determine and to enter appropriate orders and judgments, subject to review under section 158 of this title.

"(d) The district court may withdraw, in whole or in part, any case or proceeding referred under this section, on its own motion or on timely motion of any party, for cause shown. The district court shall, on timely motion of a party, so with-

draw a proceeding if the court determines that resolution of the proceeding requires consideration of both title 11 and other laws of the United States regulating organizations or activities affecting interstate commerce.

"§ 158. Appeals

"(a) The district courts of the United States shall have jurisdiction to hear appeals from final judgments, orders, and decrees, and, with leave of the court, from interlocutory orders and decrees, of bankruptcy judges entered in cases and proceedings referred to the bankruptcy judges under section 157 of this title. An appeal under this subsection shall be taken only to the district court for the judicial district in which the bankruptcy judge is serving.

"(b)(1) The judicial council of a circuit may establish a bankruptcy appellate panel, comprised of bankruptcy judges from districts within the circuit, to hear and determine, upon the consent of all the parties, appeals under subsection (a) of this section.

"(2) No appeal may be referred to a panel under this subsection unless the district judges for the district, by majority vote, authorize such referral of appeals originating within the district.

"(3) A panel established under this section shall consist of three bankruptcy judges, provided a bankruptcy judge may not hear an appeal originating within a district for which the judge is appointed or designated under section 152 of this title.

"(c) An appeal under subsections (a) and (b) of this section shall be taken in the same manner as appeals in civil proceedings generally are taken to the courts of appeals from the district courts and in the time provided by Rule 8002 of the Bankruptcy Rules.

"(d) The courts of appeals shall have jurisdiction of appeals from all final decisions, judgments, orders, and decrees entered under subsections (a) and (b) of this section.".

REPLY BRIEF

No. 10-179

Supreme Court, U.S.
FILED
JAN 11 2011
OFFICE OF THE CLERK

In The
Supreme Court of the United States

HOWARD K. STERN, EXECUTOR OF
THE ESTATE OF VICKIE LYNN MARSHALL,

Petitioner,

v.

ELAINE T. MARSHALL, EXECUTRIX OF
THE ESTATE OF E. PIERCE MARSHALL,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

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FACTUAL STATEMENT

The opposing briefs contain numerous factual distortions, some lifted from the concurrence. *See* Cert.Pet:10-11 n.4. We lack space to address every inaccuracy, but below are key clarifications:

- Pierce nonsuited Vickie from a pending state defamation action; he then filed a proof of claim for defamation seeking recovery from her bankruptcy estate, not merely a nondischargeability complaint. Pet.App:15-16 & n.11, 77, 274-76; JA:57-58; Pet.Br:3.[1] He sought to liquidate his defamation claim in the bankruptcy court, SER:6101-02, 6801, and to estimate his claim for plan confirmation, SER:8409. *Compare* Resp.Br:25; National Black Chamber of Commerce ("NBCC") Br:13, 17 & n.6; Center for the Rule of Law ("CFTRL") Br:28-30.

- Vickie asserted her tortious interference with gift claim first in the bankruptcy court, not the probate court. Pet.Br:3, 6; Cert.Pet.Reply:1-2 & n.4. *Compare* Resp.Br:20, 24.

- Vickie's bankruptcy estate benefits from the counterclaim because her reorganization

[1] Pierce describes a joint appendix document—in which he instructed Edwin Hunter to use a "shotgun approach" to filing proofs of claim, JA:55—as "privileged." Resp.Br.32. The district court admitted this document into evidence on grounds including the crime-fraud exception, Pet.App:157-58 n.25; *see* SER:8727-29, and Pierce never appealed that ruling.

plan specifies that all counterclaim proceeds are applied first to satisfy creditors. Pet.App:17; SER:6074-75, 6086. *Compare* Resp.Br:34; NBCCBr:20 n.8; CFTRLBr:28-29.

- Pierce sought to withdraw his defamation claim to the district court only after he had litigated in the bankruptcy court for twenty-seven months and faced adverse rulings; he never raised the "personal injury tort" issue in response to Vickie's summary judgment motion on his creditor's claim for defamation and never appealed the separate bankruptcy final judgment on that claim. *See* §III.A.2., *infra*. *Compare* Resp.Br:27, 70.

- Vickie properly asserted preclusion in the probate court, but that court refused to accord the bankruptcy judgment preclusive effect; her timely appeal of the probate judgment remains pending. Pet.App:223 n.4; SER:8485, 8493-94, 10306-09; 9th Cir.Docket Entry 225; Tex. 1st Ct. App. case information, http://www.1stcoa.courts.state.tx.us/opinions/case.asp?FilingID=83346 (last visited January 6, 2011). *Compare* Washington Legal Foundation ("WLF") Br:3, 10-11.

- The bankruptcy court's evidentiary sanctions for Pierce's discovery abuses are fully-supported by detailed factual findings and a lengthy appendix. Pet.App:320-26; ER:1949-57, 2235-38; D.C.Docket Entry 137: AP007986-008272. Although the district court earlier had reversed evidentiary sanctions

for lacking specific documentation, it left in place substantial monetary sanctions and stated its "preliminary" conclusion that Pierce was "stonewalling" and evidentiary sanctions were "correct." JA:128-29, 138-39. It subsequently denied Pierce's writ petition to vacate the fully-documented sanctions, SER:6720, and on de novo review of the bankruptcy judgment, it stated that had the evidence been insufficient to establish certain facts it might have deemed them established as a sanction for Pierce's discovery abuses. Pet.App:137 n.17; SER:8693-98, 8703-13. *Compare* Resp.Br:28-30, 32.

♦

ARGUMENT

I. CONGRESS INTENDED 28 U.S.C. §157(b)(2)(C) TO EMPOWER BANKRUPTCY COURTS TO DETERMINE ALL COMPULSORY COUNTERCLAIMS.

A. Vickie's Counterclaim Falls Within §157(b)(2)(C)'s Express Language.

Pierce argues that Vickie did not assert her counterclaim to Pierce's proof of claim but instead filed it against the nondischargeability complaint attached to his proof of claim. Resp.Br:52-53. That's a red herring.

Section 157(b)(2)(C) identifies as "core" all counterclaims "against persons filing claims against the estate." It does not require that counterclaims be

asserted as objections to proofs of claim. *See* Pet.App:378-79 (counterclaim captioned "Against E. Pierce Marshall," asserting jurisdiction under §157(b)(2)), 273 (district court noting/citing cases treating counterclaims as core where "asserted by procedures other than counterclaiming against the proof of claim itself").[2]

B. Pierce's "State Law" Theory Is Unfounded.

Pierce asserts that Congress' "jurisdictional scheme purposefully limits a bankruptcy court's ability to determine state law causes of action" and generally confers non-core jurisdiction over "a debtor's state law causes of action against creditors and third parties." Resp.Br:8; *see also* WLFBr:29.

But §157(b)(2) does not distinguish between counterclaims based on state law and those based on federal law. Nor does any other "core proceeding" definition listed in §157(b)(2).[3]

[2] Pierce obfuscates by stating Vickie's objections to the proof of claim "did not assert her tortious interference counterclaim" nor assert the truth defense to defamation. Resp.Br:26, 52-53. Debtors need only plead defenses under 11 U.S.C. §502(b). Vickie pled under §502(b)(1) that Pierce's claim was "unenforceable," SER:6031, thereby asserting all defenses based on applicable law, including all defenses available under nonbankruptcy law. *Travelers Cas. & Sur. Co. of Am. v. Pac. Gas & Elec. Co.*, 549 U.S. 443, 450 (2007).

[3] For example, §157(b)(2)(H) and (b)(2)(F) define as "core" all proceedings to "determine, avoid, or recover" fraudulent

(Continued on following page)

To the contrary, Congress specified in §157(b)(3) that "[a] determination that a proceeding is not a core proceeding shall not be made solely on the basis that its resolution may be affected by State law." Thus, "section 157(b)(3) restricts the use of a state-law rationale as a device to have a particular civil proceeding characterized as related. The nature or source of the cause of action, *not the governing substantive law*, is to be determinative. [¶] Nothing the Supreme Court has stated in or about [*Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982) (*Marathon*)] suggests another conclusion." 1 Collier on Bankruptcy, *supra*, ¶3.02[6][a], at 3-37 (emphasis added). In enacting §157(b)(3), Congress rejected Pierce's *Marathon* interpretation "that bankruptcy courts cannot constitutionally hear any controversy that is based upon state law." *Id.*

Pierce never *even mentions* §157(b)(3).

Moreover, Pierce's theory would gut Congress' statutory scheme. Bankruptcy courts must "consult state law in determining the validity of most claims" because "'[c]reditors' entitlements in bankruptcy

conveyances or preferences, without distinguishing actions created by 11 U.S.C. §§548 and 574 from those created by state law that vest in the trustee under 11 U S.C. §544(b). *See* 5 Alan N. Resnick & Henry J. Sommer, Collier on Bankruptcy, ¶¶544.06[2], 547.01, 548.01[2], pp. 544-20, 544-21, 547-48 n 4, 548-12, 548-13 (16th ed. 2010); *In re Mankin*, 823 F 2d 1296, 1299-1300 (9th Cir. 1987).

arise in the first instance from the underlying substantive law creating the debtor's obligation," *Travelers*, 549 U.S. at 450, and objections to claims "almost always involve state law," even avoidance actions, 1 Collier on Bankruptcy, *supra*, ¶3.02[6][a], at 3-37.

Pierce's theory also contradicts the legislative history. He references bills that were not adopted and comments by senators who opposed broad bankruptcy court jurisdiction, Resp.Br:13-17, but those views did not carry the day. Section 157 was based on a bill crafted by Representatives Kastenmeier and Kindness, who viewed *Marathon*'s constitutional strictures as narrow. *See* Pet.Br:28-31. Pierce cites snippets to suggest Kastenmeier and Kindness were concerned about "rights arising under State law" and intended to "restrict the ability of bankruptcy judges to hear state law matters." Resp.Br:17-18, 56. But Kastenmeier and Kindness distinguished between state law claims "integral to the core bankruptcy function of restructuring debtor-creditor rights" and *Marathon*-type claims. 130 Cong. Rec. 6046 (1984); *see* Pet.Br:29-31.

Pierce faults Vickie for citing Kastenmeier's and Kindness's comments in March 1984, claiming she ignores a June amendment. Resp.Br:18 n.3. But, as Kastenmeier explained, the ultimately-enacted bill rejected the Senate's attempted limitations on bankruptcy court power and "adopt[ed] the House formulation on bankruptcy court structure" with one "minor exception"—it defined "a narrow category" of proceedings (certain "personal injury tort and

wrongful death" proceedings) to be non-core, which Kastenmeier believed would "rare[ly]" result in district court adjudication. 130 Cong. Rec. 20227-20228 (June 29, 1984); *see also* 130 Cong. Rec. 20081 (June 29, 1984) (Sen. Thurmond: "the House language on the definition of core proceedings is utilized," except for the "personal injury" additions).

Pierce's implied state-law exception theory is groundless: "'[W]here Congress has intended to provide . . . exceptions to provisions of the Bankruptcy Code, it has done so clearly and expressly.'" *Travelers*, 549 U.S. at 453.

C. Pierce's Two-Step Construction Fails.

Pierce claims Congress intended a two-step approach to determining whether bankruptcy courts can finally decide "core proceedings" identified in §157(b)(2): The proceeding must (1) be "core," and (2) "arise under" the Bankruptcy Code or "arise in" the bankruptcy case. Resp.Br:51, 54.

But, as the Government explains, Pierce's two-step approach contravenes §157(b)'s plain language and statutory construction rules. Brief for the United States ("U.S.Am.Br"):18-21. It also contravenes the legislative history showing Congress used "core proceedings" to mean proceedings bankruptcy courts can finally determine, Pet.Br:29 n.12—which is how this Court has always construed the term, U.S.Am.Br:17.

Pierce accuses Vickie and the Government of "ignor[ing]" or "removing the 'arising under' and 'arising in' concepts" from the definition of core proceedings. Resp.Br:56-57. Wrong. The "core proceedings" listed in §157(b)(2) are those proceedings Congress deemed bankruptcy courts can determine *because* they "arise under" the Bankruptcy Code or "arise in" the bankruptcy case. Section 157(b)(1) does not say, as Pierce urges, "core proceedings that *also* arise under title 11 or arise in a title 11 case." Instead, it identifies two types of core proceedings—those "arising under title 11" and those "arising in a case under title 11"—differentiating them from the only other proceedings identified in §157(a), those merely "related to a case under title 11," which bankruptcy courts cannot finally determine without the parties' consent.

Pierce's assertion that Congress intended that core proceedings specified in §157(b)(2) might also be merely "related to" proceedings flouts the statutory language. "The phraseology of section 157 leads to the conclusion that there is no such thing as a core proceeding that is 'related to' a case under title 11. Core proceedings are, at most, those that arise in title 11 cases or arise under title 11." 1 Collier on Bankruptcy, *supra*, ¶3.02[2], at 3-26.

Pierce's interpretation renders much of §157(b) nonsensical. For example, Congress specified that the §157(b)(2) core proceeding list is non-exhaustive. Thus, if "core proceeding" is not shorthand for proceedings that arise under the Bankruptcy Code or

arise in the bankruptcy case, the term lacks definition and bankruptcy judges have no criteria to apply §157(b)(3)'s mandate that they determine whether proceedings are "core."

Pierce also misses the mark in his discussion of §157(b)(2)(A) and (b)(2)(O)—which define as core "matters concerning the administration of the estate" and "proceedings affecting the liquidation of the assets of the estate." Resp.Br:57-59. Courts have cautioned that a broad construction of these "catch-all" provisions could encompass the "related to" claim at issue in *Marathon* because any claim that augments the estate might conceivably "concern" estate administration or "affect" asset liquidation. *E.g*, *In re Harris*, 590 F.3d 730, 739-41 (9th Cir. 2009); *In re CBI Holdings Co.*, 529 F.3d 432, 462 & n.13 (2d Cir. 2008); *In re Meyertech Corp.*, 831 F.2d 410, 416-17 (3d Cir. 1987). Since Congress obviously did not intend a *Marathon*-type claim to be "core," courts construe the catch-all provisions narrowly to encompass only "arising under" or "arising in" matters, as Congress intended. *E.g.*, *Harris*, 590 F.3d at 739-41.

But the need to construe narrowly the ambiguous catch-all provisions does not justify engrafting restrictions onto §157(b)(2)(C)'s unambiguous language: "While the principle that constitutional problems are to be avoided in the construction of statutes is apt where a catch-all provision is at issue," the appropriate principle governing construction of §157(b)(2)(B)-(N) is that "the will of the legislature

underlying the provision is not to be ignored." *Mankin*, 823 F.2d at 1301 n.3.

Pierce also argues that "[u]nder the Government's theory, there is no such thing as a 'noncore' proceeding under section 157(b)(2)(B), and thus section 157(b)(4) would have to be ignored in its entirety." Resp.Br:59-60. Nonsense. Section 157(b)(4) provides that "[n]on-core proceedings under section 157(b)(2)(B) . . . shall not be subject to the mandatory abstention provisions of section 1334(c)(2)," and §157(b)(2)(B) deems certain personal injury tort and wrongful death proceedings to be non-core. Thus, §157(b)(4) makes mandatory abstention inapplicable to the particular tort proceedings §157(b)(2)(B) classifies as non-core. *In re Dow Corning Corp.*, 86 F.3d 482, 497 (6th Cir. 1996); *In re Pan Am Corp.*, 950 F.2d 839, 845 (2d Cir. 1991) (*Pan Am I*).

D. Vickie's Counterclaim "Arose In" The Bankruptcy Case.

Asserting that "arising in" proceedings are those "that are not based on any right expressly created by [the Bankruptcy Code], but nevertheless, would have no existence outside of bankruptcy," Pierce argues Vickie's counterclaim "obviously falls outside the scope of these standards; it is a creation of state law that could be brought in a court outside of bankruptcy." Resp.Br:55.

The legislative history confirms, however, that counterclaims and other proceedings specified in

§157(b)(2) met Congress' view of "arising under" or "arising in" proceedings because they are "proceedings integral to the core bankruptcy function of restructuring the obligations of the debtor and his creditors." 130 Cong. Rec. 6242 (Rep. Kindness); *see also* Pet.Br:28-31; 129 Cong. Rec. 9952 (April 27, 1983) (Senator Thurmond explaining mandatory abstention would not apply to proceedings "integral to the core bankruptcy function of restructuring debtor-creditor rights," including "setoffs to claims against the estate").

Ignoring the historical record of Congress' intent, Pierce instead bases his "arising in" definition on snippets from post-1984 cases that formulated their own definition of "arising in" but did not involve counterclaims. Resp.Br:55. But even cases applying that case-generated definition recognize that counterclaims to creditor claims—like the creditor claims to which they respond—"arise in" the bankruptcy case even when predicated on pre-petition state law claims. Pet.Br:27-28 & n.11. As courts rejecting Pierce's theory have explained: Such proceedings "'arise only in the context of bankruptcy,'" and although "'the state-law right underlying the claim could be enforced in a state court proceeding absent the bankruptcy, . . . the nature of the state proceeding would be different from the nature of the proceeding following the filing of a proof of claim.'" *In re Manville Forest Prods. Corp.*, 896 F.2d 1384, 1389-90 (2d Cir. 1990).

Compulsory counterclaims, in particular, "arise in" the bankruptcy case: The debtor *must* file them and they are factually and legally interconnected with the creditor's claim. Pet.Br:28.

II. SECTION 157(b)(2)(C)'S GRANT OF CORE JURISDICTION OVER ALL COMPULSORY COUNTERCLAIMS IS CONSTITUTIONAL.

Katchen/Langenkamp/Granfinanciera. Pierce attempts to distinguish *Katchen v. Landy*, 382 U.S. 323 (1966) and *Langenkamp v. Culp*, 498 U.S. 42 (1990), by arguing preference counterclaims are specially "integral to the claims allowance process" because §502(d) requires disallowance of a claim unless the creditor surrenders all preferences or fraudulent conveyances. Resp.Br:41-43. He contends §502(b) does not identify a debtor's tort claim as a disallowance ground. Resp.Br:43.

But §502(b)(1) requires disallowance of the creditor claim if it is "unenforceable . . . under applicable law," which encompasses all defenses under nonbankruptcy law and thus includes any counterclaim that offsets the claim in part or entirely. *See* n.2, *ante*; *In re R. Bastyr & Assocs., Inc.*, 81 B.R. 978, 981 n.10 (Bankr. D. Minn. 1988) (a "debtor's right of setoff" is established under state law and §502(b)(1)).

Moreover, *Langenkamp* and *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33 (1989) do not mention §502(d) or accord special status to avoidance claims. Instead, both cases turned on whether the creditor

had triggered the bankruptcy court's equitable powers over bankruptcy claims. *Langenkamp*, 498 U.S. at 44; *Granfinanciera*, 492 U.S. at 58-59. Neither case states—as Pierce suggests—that counterclaims must be "integral to claims allowance"; instead, both focus on whether the proceeding at issue arises in the claims-allowance process and thus becomes "integral to the restructuring *of the debtor-creditor relationship*." *Langenkamp*, 498 U.S. at 44 (emphasis added); *see Granfinanciera*, 492 U.S. at 58, 60 ("debtor-creditor relations").

That focus on the debtor-creditor relationship comports with the rationale of *Alexander v. Hillman*, 296 U.S. 222, 241-42 (1935) adopted in *Katchen*, 382 U.S. at 335-36, discussed in *Granfinanciera*, 492 U.S. at 59 n.14 and incorporated by reference in *Langenkamp* (citing the aforementioned *Granfinanciera* footnote discussing it, 498 U.S. at 44)—which extends the bankruptcy court's equitable power to the entire dispute between the creditor and debtor, and requires creditors, as claimants to the bankruptcy res, to account for monies owed the estate. Pet.Br:46-48.

Pierce tries to avoid *Katchen*'s adoption of *Hillman*'s rationale by claiming *Katchen* focused only on §57(g) of the Bankruptcy Act, §502(d)'s predecessor. Resp.Br:41-42. However: (1) *Katchen*, 382 U.S. at 335, expressly states that *Hillman*'s rationale "is equally applicable here"; (2) *Katchen* focused on §57(g) only because Congress had not expressly conferred summary jurisdiction on bankruptcy referees to order surrender of preferences, and the Court discerned

that intent from §57(g)'s claims-allowance connection, *id.* at 328-35; (3) §57(g) was a codification of the maxim that parties seeking equity must do equity, *In re Ft. Wayne Electric Corp.*, 99 F. 400, 402 (7th Cir. 1900), a maxim consistent with *Hillman*'s rationale; (4) this Court has rejected Pierce's narrow interpretation of *Katchen*'s scope, Pet.Br:45-46; and (5) avoidance claims (which often arise from or involve state law) are no more essential to claims allowance than compulsory counterclaims that could defeat all or part of the creditor claim.

Far from being "neither procedurally nor substantively relevant" to the allowance of Pierce's proof of claim, Resp.Br:43, Vickie's success on her counterclaim would have defeated Pierce's defamation claim, and Pierce's success on his defamation claim would have defeated her counterclaim. Pierce's assertion that "the Bankruptcy Court actually resolved Pierce's claim nearly a year before it decided Vickie's counterclaim" (based on another affirmative defense) is irrelevant. Resp.Br:42. As the Ninth Circuit held—a ruling Pierce and his amici do *not* contest—the determination whether a counterclaim is core must focus "on what is available to the court at the time of the filing, that is, the parties' pleadings." Pet.App:51-52.

Article III tests. Pierce largely ignores Vickie's explanations of why her counterclaim is constitutionally core under this Court's various tests. For example:

- He argues the Court has "made clear" that the "public rights" doctrine only applies to

"rights created by Congress" and that the adjunct theory of *Crowell v. Benson*, 285 U.S. 22 (1932) only applies to "congressionally-created rights," not state-law claims, Resp.Br:38-39, 48-49, ignoring that the core bankruptcy function of adjusting debtor-creditor relations *is* a system of congressionally-created rights, even where issues involve state law. *See Marathon*, 458 U.S. at 84 n.36 (plurality describing bankruptcy adjudications and adjustment of debtor-creditor rights as "matters of federal law").

- He quotes the *Marathon* concurrence's adjunct-court analysis as though it addressed the 1984 Act, Resp.Br:48, ignoring the structural differences between the 1978 and 1984 Acts.

- Instead of addressing constitutionality under this Court's "purposes of Article III" approach, *see* Pet.Br.50-59, he mistakenly accuses Vickie of seeking to extend the waiver analysis in *Commodity Future Trading Commission v. Schor*, 478 U.S. 833 (1986) (*Schor*), Resp.Br:45-47.[4]

[4] The amicus briefs of NBCC, WLF and law professors S. Todd Brown, et al., essentially echo Pierce's arguments. The CFTRL Brief, however, goes much farther: It argues that bankruptcy courts may not constitutionally enter final judgments on counterclaims *or claims* based on state-law actions between private parties. CFTRLBr: 3-4, 12-16, 18-26 Since "in the ordinary bankruptcy proceeding the great bulk of creditor claims are claims that have accrued under state law," *Marathon*, 458 U.S at 96 (White, J., dissenting), CFTRL's theory would effectively

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III. PIERCE'S "PERSONAL INJURY TORT" ARGUMENT IS NO BASIS TO AFFIRM THE NINTH CIRCUIT JUDGMENT.

A. Pierce Waived/Forfeited His "Personal Injury Tort" Argument.

1. Creditors can waive/forfeit objections to bankruptcy courts entering final orders on "personal injury tort or wrongful death" claims.

Pierce argues that the bankruptcy court lacked "jurisdiction" over his defamation claim and therefore lacked "jurisdiction" to determine Vickie's compulsory counterclaim. Resp.Br:35-36, 65-71. His argument confuses subject matter jurisdiction with the classification of proceedings as core/non-core.

District and bankruptcy courts have subject matter jurisdiction over all bankruptcy cases and all proceedings arising under the Bankruptcy Code or arising in or related to bankruptcy cases. 28 U.S.C. §§1334(b), 157(a); *Celotex Corp. v. Edwards*, 514 U.S. 300, 307-08 (1995). Parties cannot waive, forfeit or expand that jurisdiction. *In re Mullarkey*, 536 F.3d 215, 222 (3d Cir. 2008).

In contrast, "'[t]he classification of a proceeding as core or noncore does not determine the jurisdiction of a bankruptcy court, but instead relates to a

render the entire bankruptcy scheme unconstitutional and invalidate over a century of bankruptcy practice.

determination of whether the court may enter a final order or judgment. . . .'" 1 William L. Norton, Jr., Norton Bankruptcy Law and Practice §4:30, 4-124 (3d ed. 2010). It concerns the right to adjudication by an Article III judge, a personal right that can be willingly relinquished or waived/forfeited by litigation conduct, just like the jury-trial right. *Schor*, 478 U.S. at 849 (failure to object until after adverse ruling); *Roell v. Withrow*, 538 U.S. 580, 583, 590 (2003) (consent to magistrate's final judgment inferred from party's failure to timely assert right to refuse final adjudication).

Consequently, parties to bankruptcy proceedings can consent to bankruptcy courts entering final judgment on non-core matters. §157(c)(2); *In re OCA, Inc.*, 551 F.3d 359, 368 (5th Cir. 2008). And, they can waive/forfeit objections to bankruptcy courts entering final orders on non-core matters, by failing to assert—clearly and promptly—a right to Article III adjudication or by objecting to bankruptcy court adjudication as non-core only after adverse rulings. *Id.* at 368-69; *In re Tx. Gen. Petroleum Corp.*, 52 F.3d 1330, 1337 (5th Cir. 1995) (citing cases).[5]

[5] Bankruptcy parties can similarly waive/forfeit a right to jury trial (Pierce never requested one) by failing to file a jury-trial demand shortly after service of the last relevant pleading. Fed R. Bankr. P 9015, 5005; Fed. R Civ P. 38(b), (d); *In re Yukon Energy Corp.*, 138 F.3d 1254, 1260 (8th Cir. 1998) Even parties filing timely jury demands can subsequently waive/forfeit their right by waiting too long to seek withdrawal to the

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Parties also waive/forfeit the right to contest a bankruptcy court's entry of a final judgment on a non-core matter by "'failing to raise or pursue the issue adequately on appeal,'" including by failing to appeal in the district court before launching an attack in the circuit court. *Mullarkey*, 536 F.3d at 221; *Yukon*, 138 F.3d at 1258; *see also* §157(c)(1) (confining district court de novo review of bankruptcy court decisions in non-core proceedings to "matters to which any party has timely and specifically objected").[6]

Although Vickie unequivocally raised the issue during the certiorari petition process (Cert.Pet. Reply:12-13), Pierce's brief ignores the waiver/forfeiture issue. Instead, Pierce suggests bankruptcy courts can never adjudicate personal injury tort claims by characterizing §157(b)(5)'s "shall be tried in the district court" language as mandatory. Resp.Br:66.[7] But "[s]ection 157(b) generally, and Section 157(b)(5) in particular, do not create or destroy jurisdiction." *In re Smith*, 389 B.R. 902, 912

district court. *In re HA-LO Indus.*, 326 B.R. 116, 122 (Bankr. N.D. Ill. 2005).

[6] Circuit courts in bankruptcy cases have jurisdiction only over district court judgments; parties can therefore waive circuit court challenges to bankruptcy court judgments by failing to seek district court review. *Brandt v. Wand Partners*, 242 F.3d 6, 14-15 (1st Cir. 2001); *In re Andy Frain Servs., Inc.*, 798 F.2d 1113, 1124 (7th Cir. 1986).

[7] He later equivocates, noting personal injury claims can be tried in state court. Resp.Br:66-67; *see Pan Am I*, 950 F.2d at 844 ("Despite the mandatory 'shall order,' section 157(b)(5) has consistently been construed to recognize discretion in district courts to leave personal injury cases where they are pending").

(Bankr. D. Nev. 2008).[8] Section 157(b)(5) is a venue-fixing provision that situates the bankruptcy jurisdiction already conferred upon federal courts. *Id.*[9] Such case-processing provisions can always be waived. *Kontrick v. Ryan*, 540 U.S. 443, 456 (2004); *United Student Aid Funds, Inc. v. Espinosa*, 130 S. Ct. 1367, 1380 (2010).[10] Representative Kastenmeier confirmed the nonjurisdictional nature of §157(b)(5) by acknowledging that bankruptcy courts can determine personal injury torts "with the consent of all parties." 130 Cong. Rec. 20228 (June 29, 1984).

Thus, "personal injury tort" proceedings are subject to the same waiver/forfeiture principles as all

[8] Notably, as one bankruptcy judge has explained in detail, "[s]ection 157(b)(5) is not worded as Congress might normally construct a restrictive jurisdictional statute." *Smith*, 389 B.R. at 911. Where Congress has not explicitly designated a statute jurisdictional, it must be deemed nonjurisdictional. *Arbaugh v. Y & H Corp.*, 546 U.S. 500, 515-16 (2006).

[9] A primary purpose of §157(b)(5) is to empower the district court to centralize in one federal court all personal injury tort actions pending against the debtor in federal and state courts *Dow Corning*, 86 F.3d at 495-97; *In re Pan Am Corp.*, 16 F.3d 513, 516 (2d Cir. 1994) ("Congress enacted section 157(b)(5) to expand the district court's venue-fixing powers").

[10] In suggesting bankruptcy courts can never adjudicate personal injury tort proceedings, Pierce quotes sweeping language in *Pettibone Corp. v. Easley*, 935 F.2d 120, 123 (7th Cir. 1991). Resp.Br:65-66. That language is dicta and has been criticized as "the most egregious misapplication of *Marathon*." *In re Downing Corp* , 215 B.R. 346, 353 (Bankr. E.D. Mich. 1997); *see In re UAL Corp.*, 310 B.R 373, 379 (Bankr. N.D. Ill. 2004). *Pettibone* does not address the waiver/forfeiture issue.

other non-core proceedings. *Smith*, 389 B.R. at 906-16 (creditor waived right to contest bankruptcy court entering final judgment on non-core defamation claim by, as here, filing proof of claim for defamation and a complaint seeking nondischargeability that alleged the adversary proceeding was core, and not filing a jury-trial demand); *In re Leslie Fay Cos.*, 212 B.R. 747, 772-73 (Bankr. S.D.N.Y. 1997) (failure to timely raise personal injury issue to bankruptcy court), *aff'd*, 222 B.R. 718 (S.D.N.Y. 1998), *aff'd*, 82 F.3d 899 (2d Cir. 1999); *Adams v. Cumberland Farms, Inc.*, 86 F.3d 1146, at *3 (1st Cir. 1996) (unpublished table decision) (circuit court argument waived by failure to raise personal injury argument in bankruptcy court and opening brief to district court).

2. Pierce's waiver/forfeiture.

a. Pierce litigated his claim in the bankruptcy court for twenty-seven months before seeking withdrawal in response to adverse rulings.

Parties to adversary proceedings must state in their pleadings whether a proceeding is core or non-core and whether they consent to the bankruptcy judge finally determining any non-core matter. Fed. R. Bankr. P. 7008(a), 7012(b). Pierce never alleged non-core jurisdiction. In fact, the only pleading attached to the proof of claim and incorporated by reference—Pierce's previously-filed dischargeability complaint—alleged that the adversary proceeding was "a core proceeding" and raised no distinction

between the nondischargeability request and the underlying defamation claim. Pet.App:81. And although Pierce emphasizes that "when [he] filed his proof of claim, he expressly indicated that his defamation action constituted a personal injury tort," Resp.Br:25, 68, all he did was check a box on a preprinted form, which merely identified the claim's basis and contained no statutory references or indication that the claim was non-core or that he did not consent to final bankruptcy court adjudication, Pet.App:78.

Indeed, Pierce expressly told the bankruptcy court that "[a]ll parties are in agreement that *the amount* of the contingent Proof of Claim filed by [Pierce] shall be determined by the adversary proceedings filed herein" and that he would be "happy" and "pleased" to litigate "[his] claim here" because "we did choose this forum." SER:6101-02, 6801 (emphasis added). The district court recognized that Pierce thereby consented to the bankruptcy court adjudicating his defamation claim. Pet.App:266-67 n.17.

Pierce distorts the record when he sweepingly asserts that he "repeatedly raised section 157(b)(5) below." Resp.Br:70. Tellingly, he cites only his September 1998 motion under §157(d) to withdraw the entire litigation to the district court and jurisdictional arguments he made in his Ninth Circuit appeal. Resp.Br:70; *see id.* at 26-27; JA:95. He omits that he first sought withdrawal only after extensively adjudicating his claim in the bankruptcy court *for*

twenty-seven months and he was facing the bankruptcy court's imposition of substantial monetary and potentially terminating discovery sanctions. *See* JA:117-21; ER:1949-57, 2235-38; D.C.Docket Entry 137:AP007986-008272; Pet.Br:4 n.4.

Although the district court initially withdrew Pierce's defamation claim and Vickie's counterclaim, it shortly referred them back to the bankruptcy court to be tried, relying among other things on "judicial economy," the "immersion that the bankruptcy judge has in this case," and Pierce's "selection of forum," stressing that "much of what we see here is the spawn of what he begot." JA:129-30, 138-39.

That decision was a proper exercise of discretion. Parties must seek withdrawal "'as promptly as possible in light of the developments in the bankruptcy proceeding'" and district courts must consider "the efficient use of judicial resources, delay and costs to the parties, uniformity of bankruptcy administration, the prevention of forum shopping, and other related factors." *Sec. Farms v. Int'l Broth. of Teamsters, Chauffers, Warehousemen & Helpers*, 124 F.3d 999, 1007 n.3, 1008 (9th Cir. 1997); *see* §157(d) (motion must be "timely"). The timeliness requirement prevents parties "'from forum shopping, stalling, or otherwise engaging in obstructionist tactics,'" including extensively litigating matters in the bankruptcy court long after the alleged ground for withdrawal was known and seeking withdrawal because of adverse rulings—exactly what Pierce did. *In re Childs*, 342 B.R. 823, 828-30 (M.D. Ala. 2006) (citing cases); *In re GTS 900*

F, LLC, No. CV10-06693 SJO, 2010 WL 4878839, at *2-3 (C.D. Cal. 2010) (citing cases).

b. Pierce never appealed the bankruptcy court's entry of final judgment on his defamation claim.

After the district court returned the defamation claim to the bankruptcy court, Pierce never raised the "personal injury tort" exception in the bankruptcy court:

- When Vickie moved for summary judgment on the defamation claim, Pierce opposed on the merits and never argued that the "personal injury tort" exception precluded that court from entering final judgment. D.C.Docket Entry 140:AP009614-009668, AP009722-009736.
- After the bankruptcy court entered a separate final judgment dismissing the defamation claim, Pierce never appealed that judgment. SER:7940-42, 8086-87; Fed. R. Bankr. P. 8002; 28 U.S.C. §158(a), (b), (c)(2).
- When the bankruptcy court subsequently tried Vickie's counterclaim, Pierce never argued that the bankruptcy court lacked core jurisdiction over the counterclaim because the "personal injury tort" exception made his defamation claim non-core. D.C.Docket Entries 152:AP016108-016147, 159:AP019936-019979, 162:AP019777-019818, 165:AP022062-022088.

- After the bankruptcy court entered a separate judgment on Vickie's counterclaim, Pierce appealed only that judgment. Pet.App:300-04; D.C.Docket Entry 172:AP025768-02570, AP026129-026132.

The absence of an appeal from the bankruptcy court's entry of final judgment on Pierce's defamation claim makes that adjudication final, thereby precluding Pierce's argument that the adjudication of the defamation claim was non-core and that therefore Vickie's counterclaim was non-core.

Further, in his appeals to the district court and Ninth Circuit, Pierce never attempted to counter the undisputed record of his waiver/forfeiture or contest the district court's discretionary decision to vacate withdrawal of the defamation claim. Instead, he hung his hat—as he does now—on the erroneous notion that the "personal injury issue" can never be waived/forfeited.[11]

[11] In response to the district court's decision to vacate withdrawal, Pierce filed a writ of mandate in the Ninth Circuit, arguing withdrawal was mandatory because the bankruptcy court lacked subject matter jurisdiction over personal injury claims and, alternatively, that the district court abused its discretion. D.C.Docket Entry 97:CA0001-0026. After the Ninth Circuit summarily denied the writ, SER:5982, Pierce never again raised the latter argument; he argued only his erroneous jurisdictional argument

B. Pierce's Defamation Claim Was Not A "Personal Injury Tort Or Wrongful Death" Proceeding Under §157(b).

Because parties can waive/forfeit the right to refuse or contest final adjudication by a bankruptcy court, and the undisputed record establishes such waiver/forfeiture by Pierce, this Court need not determine whether his defamation claim falls within the "personal injury tort" exception. We therefore address the issue only briefly.

Pierce argues that this Court should broadly construe §157(b)'s "personal injury tort" language because "where Congress intends to narrow 'personal injury torts' to those involving bodily injury, it does so expressly," and since "Congress did not impose such a limitation in §157(b)(5), the term should be given its ordinary, intended meaning." Resp.Br:69-70.

But §157(b) does not only refer to "personal injury tort" claims. It says "personal injury tort [and/or] *wrongful death* claims." *See* §157(b)(2)(B), (O), (b)(5) (emphasis added.) Wrongful death claims stem from bodily injury. Under the *ejusdem generis* doctrine, the inclusion of that language indicates Congress intended a narrow concept of "personal injury tort." Moreover, the legislative history confirms that a narrow scope was intended. Representative Kastenmeier described the personal injury tort/ wrongful death exception as a "minor exception" encompassing only "a narrow category of cases," 130 Cong. Rec. 20228, and the only torts specifically

identified in §157(b)(2)(B)'s legislative history are "claims arising from automobile accidents," 130 Cong. Rec. 17155.

Thus, the legislative history and usage of the phrase "personal injury tort or wrongful death" indicates Congress did *not* intend the exception to apply broadly but only to traditional personal injury torts involving physical impact or trauma (the type that could lead to wrongful death), such as automobile accidents, slip and falls, and products liability. *See, e.g., In re Atron Inc. of Mich.*, 172 B.R. 541, 543-45 (Bankr. W.D. Mich. 1994). Accordingly, defamation claims have been held to fall outside the exception. *Massey Energy Co. v. W. Va. Consumers for Justice*, 351 B.R. 348, 351 (E.D. Va. 2006); *In re Davis*, 334 B.R. 874, 878 n.2 (Bankr. W.D. Ky. 2005), *aff'd in part, rev'd in part on other grounds*, 347 B.R. 607 (W.D. Ky. 2006).[12]

[12] Pierce erroneously cites 11 U.S.C §522(d)(11)(D) for the principle that Congress always uses the term "bodily" to narrow personal injury torts to physical-impact torts. Resp.Br:69. But §522(d)(11)(D) is not a personal injury tort statute, nor does it reference "wrongful death " Instead, it lets debtors exempt from the bankruptcy estate certain payments "on account of [the debtor's] personal bodily injury," excluding mental anguish and pecuniary loss, *i.e* , loss-of-limb type payments that can come from any source, including insurance or workers' compensation Moreover, bankruptcy statutes often use "wrongful death" and "personal injury" together when unmistakably intending to mean only physical-impact injuries. *E.g.*, 11 U.S.C. §§523(9) ("death or personal injury" caused by operation of vehicle),

(Continued on following page)

Regardless, Pierce's particular defamation claim falls outside even a broader construction. Pierce concedes that the "personal injury tort" exception "rests on grounds of fairness," emphasizing Senator DeConcini's comments that "'[u]nlike a trade creditor who elects to do business with a particular company, the personal injury tort claimant does not choose to be injured by a particular debtor.'" Resp.Br:67-68. DeConcini emphasized that with the latter torts, the injury "just happened." 130 Cong. Rec. 13076. Courts have relied on such comments to extend §157(b) beyond physical-impact torts but not to torts bearing "earmarks of a financial, business or property tort claim, or a contract claim"—an approach that requires a "searching analysis of the complaint." *In re Ice Cream Liquidation, Inc.*, 281 B.R. 154, 161 (Bankr. D. Conn. 2002).

Pierce's defamation claim is not a tort between strangers occurring out of the blue, such as a dispute between a private citizen and newspaper columnist. *Compare Smith*, 389 B.R. at 905-06. It stems from a financial dispute between a mother-in-law and son-in-law over alleged interference with her right to receive property from her husband. It's a family battle over money, not a random tort between strangers that "just happened."

•

524(g)(2)(B)(i)(I) ("personal injury, wrongful death" from asbestos).

CONCLUSION

The Ninth Circuit erred in holding that the bankruptcy court lacked core jurisdiction over Vickie's compulsory counterclaim. This Court therefore should remand the case to the district court, because that court erroneously treated the proceeding as non-core and has not yet reviewed it under the correct, more deferential standard.

Dated: January 10, 2011

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AMICUS CURIAE BRIEF

Supreme Court, U.S.
FILED
NOV 19 2010
OFFICE OF THE CLERK

No. 10-179

In the Supreme Court of the United States

HOWARD K. STERN, EXECUTOR OF THE ESTATE OF VICKIE LYNN MARSHALL, PETITIONER

v.

ELAINE T. MARSHALL, EXECUTRIX OF THE ESTATE OF E. PIERCE MARSHALL

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE SUPPORTING PETITIONER

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QUESTIONS PRESENTED

Whether, consistent with 28 U.S.C. 157 and Article III, a bankruptcy judge may enter final judgment on a bankruptcy estate's compulsory counterclaim against a bankruptcy claimant, even when adjudication of the counterclaim requires resolution of issues that are not implicated by the claim against the estate.

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In the Supreme Court of the United States

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HOWARD K. STERN, EXECUTOR OF THE ESTATE OF VICKIE LYNN MARSHALL, PETITIONER

v.

ELAINE T. MARSHALL, EXECUTRIX OF THE ESTATE OF E. PIERCE MARSHALL

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BRIEF FOR THE UNITED STATES AS AMICUS CURIAE SUPPORTING PETITIONER

INTEREST OF THE UNITED STATES

This case presents the question whether Congress has authorized, and may constitutionally authorize a district court to refer to a bankruptcy judge the final adjudication of a compulsory counterclaim by a bankruptcy estate against a creditor who has filed a claim against the estate. The United States has a substantial interest in the outcome of the case because United States trustees—who are Department of Justice officials appointed by the Attorney General—supervise the administration of bankruptcy cases. See 28 U.S.C. 581-589a (2006 & Supp. II 2008). See also 11 U.S.C. 307 ("The United States trustee may raise and may appear

and be heard on any issue in any [bankruptcy] case or proceeding."). The United States also has a substantial interest in this case because, although the court of appeals framed its holding as one of statutory construction, the court's analysis calls into question the scope of Congress's constitutional authority to authorize bankruptcy-judge adjudication of counterclaims filed by the estate. Cf. 28 U.S.C. 2403(a) (authorizing the United States to intervene in "any action, suit, or proceeding in a court of the United States * * * wherein the constitutionality of any Act of Congress affecting the public interest is drawn into question").

STATEMENT

1. Article I of the Constitution assigns to Congress the "Power * * * To establish * * * uniform Laws on the subject of Bankruptcies throughout the United States." U.S. Const. Art. I, § 8, Cl. 4. In exercising its plenary authority to regulate bankruptcy, Congress has given "special attention to the subject of making the bankruptcy laws inexpensive in their administration." *Katchen* v. *Landy*, 382 U.S. 323, 328 (1965) (quoting H.R. Rep. No. 1228, 54th Cong., 1st Sess. 2 (1896); S. Rep. No. 1916, 75th Cong., 3d Sess. 2 (1938)) (alterations omitted). To that end, it has both created specialized fora for the adjudication of bankruptcy matters and provided that such matters may be resolved summarily without a jury.

a. 1898 Bankruptcy Act, Ch. 541, 30 Stat. 544, vested district courts with original jurisdiction as "courts of bankruptcy," *id.* § 2, 30 Stat. 545, and empowered them to refer cases in whole or in part to bankruptcy "referees," *id.* § 22a, 30 Stat. 552. Those referees (later renamed "bankruptcy judges") were appointed by

district courts for two-year terms and were removable by those courts for cause. *Id.* § 34, 30 Stat. 555. They were authorized, with certain exceptions, to "perform such part of the duties * * * as are by this Act conferred on courts of bankruptcy," "subject always to a review by the [district] judge." *Id.* § 38, 30 Stat. 555.

In 1973, this Court prescribed Bankruptcy Rules pursuant to 28 U.S.C. 2075. See 411 U.S. 995. Rule 102 provided for the automatic referral of all bankruptcy proceedings to a referee, while authorizing the district court to withdraw such a reference "for the convenience of the parties or other cause" on a case-by-case basis. *Id.* at 1003-1004. The set of proceedings committed to the referee for adjudication in the first instance included "counterclaims against a creditor who files claims against the estate." *Northern Pipeline Const.* v. *Marathon Pipe Line Co.*, 458 U.S. 50, 99 (1982) (White, J. dissenting); see 1973 Bankr. R. 306(c), 701 & advisory cmte. note. Cf. *Katchen*, 382 U.S. at 336 n.12 (noting pre-1973 appellate decisions "upholding summary jurisdiction to grant affirmative relief on related counterclaims that would also be defenses to [a creditor's] claim"). Rule 803 stated that "the judgment or order of the referee shall become final" unless appealed. 411 U.S. at 1088. On appeal, the district court was required to "accept the referee's findings of fact unless clearly erroneous." 1973 Bankr. R. 810, 411 U.S. at 1090.

b. The Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549, sought to "substantially expand[]" bankruptcy jurisdiction and to enlarge the role of specialized bankruptcy fora. H.R. Rep. No. 595, 95th Cong., 1st Sess. 13 (1977). Under the 1978 Act, the power to enter final judgment in all "civil proceedings arising under title 11 or arising in or related to cases under title

11" was vested in a set of newly created "United States Bankruptcy Courts," which replaced referees. 28 U.S.C. 151(a), 1471(b) and (c) (Supp. IV 1980). Judges of those new bankruptcy courts were appointed for 14-year terms by the President, with the advice and consent of the Senate. 28 U.S.C. 152 (Supp. IV 1980). Review of bankruptcy-court judgments was solely appellate in nature. 28 U.S.C. 160, 1334 (1976 & Supp. IV 1980).

The constitutionality of the 1978 Act was challenged shortly after its enactment. In *Northern Pipeline*, a bankrupt debtor attempted to prosecute various state-law claims in bankruptcy court against a company that had never made a claim against the debtor's estate or otherwise appeared in the bankruptcy proceedings. 458 U.S. at 56-57 (plurality opinion). This Court held that the bankruptcy court's exercise of jurisdiction over that suit conflicted with the requirement of Article III, Section 1 that "[t]he judicial Power of the United States shall be vested" in judges who have life tenure and protection from salary reduction. See *id.* at 88 & n.40 (plurality opinion); *id.* at 91 (Rehnquist, J., concurring in the judgment).

As this Court subsequently explained, although a majority of the Justices in *Northern Pipeline* agreed that the 1978 Act was unconstitutional as applied to the suit before it, the "divided Court was unable to agree on the precise scope and nature of Article III's limitations." *Thomas* v. *Union Carbide Agric. Prods. Co.*, 473 U.S. 568, 584 (1985). "The Court's holding in" *Northern Pipeline* therefore "establishes only that Congress may not vest in a non-Article III court the power to adjudicate, render final judgment, and issue binding orders in a traditional contract action arising under state law, without consent of the litigants, and subject only to ordi-

nary appellate review." *Ibid.* Nevertheless, six Justices concluded that the statutory authorization for the bankruptcy court to adjudicate the state-law contract action at issue in the case was not severable from the remainder of the 1978 Act's grant of jurisdiction to bankruptcy courts, and the Court accordingly struck down the entire jurisdictional grant as unconstitutional. *Northern Pipeline*, 458 U.S. at 88 & n.40, 91-92 (plurality opinion); *id.* at 91-92 (Rehnquist, J., concurring in the judgment). The Court stayed its judgment for approximately three months to "afford Congress an opportunity to reconstitute the bankruptcy courts or to adopt other valid means of adjudication, without impairing the interim administration of the bankruptcy laws." *Id.* at 88 (plurality opinion); *id.* at 92 (Rehnquist, J., concurring in the judgment).

c. The Judicial Conference of the United States, concerned that Congress might not act before the Court's stay expired, requested that the Director of the Administrative Office of the United States Courts (Director) propose a rule for adoption by the courts that would allow for the continued operation of the bankruptcy system consistent with *Northern Pipeline*. Judicial Conf. of United States, *Report of Proceedings* 91 (Sept. 1982). The Director responded by circulating a memorandum and proposed rule setting forth "an interim measure, by which district courts may delegate many of their bankruptcy powers to bankruptcy judges." Memorandum from William E. Foley, Director, Administrative Office of the United States Courts (Dec. 3, 1982) (Foley Memorandum), reprinted in *Bankruptcy Court Act of 1983: Hearing on H.R. 3 Before the Subcomm. on Monopolies and Commercial Law of the Comm. on the Judiciary*, 98th Cong. 1st Sess. 160 (1983)

(*1983 Subcomm. Hearing*). When Congress ultimately failed to act before this Court's stay expired, a revised version of the Director's proposed rule was adopted, "with minor local variations," by all of the courts of appeals and district courts. Vern Countryman, *Scrambling To Define Bankruptcy Jurisdiction: The Chief Justice, the Judicial Conference, and the Legislative Process*, 22 Harv. J. Legis. 1, 23 (1985).

The interim rule scaled back the jurisdiction that the 1978 Act had conferred upon bankruptcy judges. Rather than vesting bankruptcy judges with original jurisdiction over "[a]ll cases under Title 11 and all civil proceedings arising under Title 11 or arising in or related to cases under Title 11," the interim rule provided that such matters would be "referred" to bankruptcy judges by the district court. Interim Bankr. R. § (c)(1), reprinted in *1983 Subcomm. Hearing* 161-163 (reproduced in the appendix). It additionally specified that such references could be withdrawn in whole or in part by the district court "at any time on its own motion or on timely motion by a party," and that the district court could review de novo a bankruptcy judge's determinations. *Id.* § (c)(2), (e)(2).

The interim rule also precluded bankruptcy judges from entering final judgment in a class of proceedings that the Director dubbed "*Marathon* claims" and in the rule were called "related proceedings." Foley Memorandum; Interim Bankr. R. § (d)(3)(B). The rule provided that in such proceedings a bankruptcy judge would simply "submit findings, conclusions, and a proposed judgment or order to the district judge" unless the parties consented to a different allocation of authority between the bankruptcy and district judges. *Ibid.* In other referred matters, however, a bankruptcy judge

could enter final judgment. *Id.* § (d)(2). The set of proceedings in which bankruptcy courts could exercise that final-judgment authority included, *inter alia*, "counterclaims by the estate in whatever amount against persons filing claims [against] the estate." *Id.* § (d)(3)(A).

During the period that it was in effect, the interim rule was uniformly upheld against constitutional challenge by the courts of appeals. *Salomon* v. *Kaiser*, 722 F.2d 1574, 1581 (2d Cir. 1983); *Braniff Airways, Inc.* v. *Civil Aeronautics Bd.*, 700 F.2d 214, 215 (5th Cir.) (per curiam), cert. denied, 463 U.S. 1208 (1983); *White Motor Corp.* v. *Citibank, N.A.*, 704 F.2d 254, 263 (6th Cir. 1983); *Stewart* v. *Stewart*, 741 F.2d 127, 131 (7th Cir. 1984); *First Nat'l Bank of Tekamah* v. *Hansen*, 702 F.2d 728, 729 (8th Cir.), cert. denied, 463 U.S. 1208 (1983) (per curiam); *Lindquist* v. *Metropolitan Bank*, 730 F.2d 1204, 1205 (8th Cir. 1984) (per curiam); *Oklahoma Health Servs. Fed. Credit Union* v. *Webb*, 726 F.2d 624, 625 (10th Cir. 1984); *In re Colorado Energy Supply, Inc.*, 728 F.2d 1283, 1284-1285 (10th Cir. 1984); *Committee of Unsecured Creditors of F S Commc'ns Corp* v. *Hyatt Greenville Corp.*, 760 F.2d 1194, 1198-1199 (11th Cir. 1985).

d. Just over two years after this Court's decision in *Northern Pipeline*, Congress enacted the Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 333, which laid the foundation for the current bankruptcy system. The primary sponsor of the 1984 Act's jurisdictional provisions explained that those provisions were intended to codify the practice under the Judiciary's interim rule:

> The solution offered by my amendment has been at work in the last 18 months under the emergency bankruptcy rule known as the model rule and has

> been upheld by five circuit courts of appeal and 24 district courts. It has proven successful. Nothing need be changed. Congressional enactment of the model rule is the purpose of my amendment, and that is all that is necessary.

130 Cong. Rec. 6241 (1984) (statement of Rep. Kastenmeier); see *id.* at 6242 (statement of Rep. Kindness) ("The Kastenmeier-Kindness amendment is essentially a legislative enactment of the emergency bankruptcy rule, the model rule that has been in effect, under which the bankruptcy courts have been operating. It has been ruled constitutional by five circuits now, every place where the question has been raised. The Supreme Court has passed up the opportunity to review those cases.").

The 1984 Act vests the district courts with original jurisdiction over bankruptcy matters. 28 U.S.C. 1334(a)-(b). It further provides that district courts "may," as under the interim rule, "provide that any or all cases under title 11 and any or all proceedings arising under title 11 or arising in or related to a case under title 11 may be referred to the bankruptcy judges for the district." 28 U.S.C. 157(a). Under the 1984 Act (as under the interim rule), a district court "may withdraw, in whole or in part, any case or proceeding referred under this section, on its own motion or on timely motion of any party, for cause shown." 28 U.S.C. 157(d).

Also like the interim rule, the 1984 Act authorizes bankruptcy judges to enter final judgments in some types of proceedings but not others. In particular, bankruptcy judges may enter final judgments in "all core proceedings arising under title 11, or arising in a case under title 11," that are referred to them by a district court. 28 U.S.C. 157(b)(1). Bankruptcy courts' judgments in such proceedings are subject to appellate re-

view by district courts, bankruptcy appellate panels, and circuit courts of appeals. See 28 U.S.C. 158. If a particular proceeding "is not a core proceeding but * * * is otherwise related to a case under title 11," however, a bankruptcy judge may not enter final judgment, but may instead submit proposed findings of fact and conclusions of law to the district court for de novo review. 28 U.S.C. 157(c)(1). The 1984 Act states that "[c]ore proceedings include, but are not limited to," various enumerated matters. 28 U.S.C. 157(b)(2). Those matters include "counterclaims by the estate against persons filing claims against the estate." 28 U.S.C. 157(b)(2)(C).

The 1984 Act also altered the manner in which bankruptcy judges are appointed. Those judges are no longer selected by the President (as they were under the 1978 Act), but instead are appointed by the courts of appeals for the circuits in which their judicial districts are located. 28 U.S.C. 152(a)(1). They "serve as judicial officers of the United States district court established under Article III of the Constitution." *Ibid.*

2. a. In 1996, Vickie Lynn Marshall (referred to interchangeably with the executor of her estate as "petitioner") filed for Chapter 11 bankruptcy relief in the Central District of California. Pet. App. 13. By local rule, the district court in the Central District of California "refers to the bankruptcy judges of this district, all cases under Title 11 and all proceedings under Title 11 or arising in or related to a case under Title 11." Gen. Order 266 (C.D. Cal. Oct. 9, 1984).

Petitioner's stepson, E. Pierce Marshall (referred to interchangeably with the executrix of his estate as "respondent"), filed a proof of claim in petitioner's bankruptcy case. Pet. App. 15. As construed by the courts below, that claim sought damages for alleged defama-

tory statements by petitioner and her attorneys to the effect that respondent had tortiously interfered with petitioner's rights in the estate of her recently deceased husband (respondent's father). *Id.* at 14-15 & n.11, 274-276. Petitioner answered the adversary complaint by asserting, *inter alia*, that she could not be held liable for defamation because the relevant statements were true. *Id.* at 16. Petitioner also filed a counterclaim for "tortious interference with her rights as [her late husband's] spouse." *Ibid*

The bankruptcy judge presiding over petitioner's Chapter 11 case held a trial. Pet. App. 18. It granted summary judgment for petitioner on respondent's defamation claim. *Ibid.* The bankruptcy court also found in petitioner's favor on petitioner's counterclaim, determining that respondent had tortiously interfered with petitioner's expectation in her late husband's estate. *Ibid.* The bankruptcy court determined that it had jurisdiction under 28 U.S.C. 157 to finally adjudicate the counterclaim. Pet. App. 294-296. In December 2000, it entered final judgment for petitioner in the total amount of $474,754,134. *Id.* at 301.

b. Respondent appealed to the district court. Pet. App. 24. The district court vacated the judgment on the ground that petitioner's tortious-interference counterclaim was not the type of matter on which bankruptcy judges may enter final judgment. *Id.* at 283. The district court acknowledged that the counterclaim "falls within the literal language of [28 U.S.C.] § 157(b)(2)(C)." *Id.* at 276. Based largely on perceived constitutional concerns, however, the court concluded that the counterclaim was too far attenuated from respondent's defamation claim to allow for decision by the bankruptcy judge. See *id.* at 265-283. The district court therefore treated

the bankruptcy court's ruling as a *proposed* judgment subject to the district court's own independent review. *Id.* at 284; see 28 U.S.C. 157(c)(1).

c. During the pendency of the federal-court proceedings, petitioner and respondent were also participating in Texas probate-court proceedings concerning administration of the estate of petitioner's late husband, respondent's father. Pet. App. 11-13, 20. In the state court, respondent sought a declaration that his father's will and living trust were valid. *Id.* at 11. Petitioner challenged the validity of those instruments and sought recovery from respondent for tortious interference on essentially the same theory that she pressed in the bankruptcy court. *Id.* at 11-12.

After the bankruptcy court entered judgment in her favor, petitioner voluntarily dismissed her pending claims in the Texas probate proceedings. Pet. App. 20-21. Petitioner remained a party to the Texas proceedings, however, as a defendant in a declaratory judgment action brought by respondent to determine their respective rights to the decedent's estate. *Id.* at 21. Following a lengthy trial, the jury found that the will and trust were valid, and that petitioner did not in fact have a legitimate expectation of rights in the decedent's estate. *Id.* at 22. In December 2001, the Texas probate court entered an amended judgment in favor of respondent on all claims. *Id.* at 22-23.

d. When the Texas probate court entered that judgment, the district court was in the midst of its independent review of the bankruptcy court's decision on petitioner's tortious-interference counterclaim. Pet. App. 219, 222. Relying on principles of issue preclusion and res judicata, respondent filed a motion for summary

judgment, which the district court denied. *Id.* at 217-234.

The district court proceeded to take additional evidence on petitioner's counterclaim. Pet. App. 25. In March 2002, it issued a lengthy opinion agreeing with the bankruptcy court that respondent had committed tortious interference. *Id.* at 90-214. It entered judgment in petitioner's favor, awarding a total of $88,585,534.66. *Id.* at 216.

e. Both parties appealed the district court's decision. Pet. App. 26. The court of appeals vacated the district court's judgment, holding that the probate exception to federal jurisdiction precluded the federal courts from adjudicating the case. *Marshall* v. *Marshall*, 392 F.3d 1118 (9th Cir. 2004). This Court reversed and remanded for consideration of additional issues, including the bankruptcy judge's jurisdiction to enter final judgment and respondent's arguments of issue and claim preclusion. *Marshall* v. *Marshall*, 547 U.S. 293, 315 (2006).

f. On remand, the court of appeals reversed the district court's judgment and ordered entry of judgment in favor of respondent. Pet. App. 5. The court of appeals concluded that "the Texas probate court's judgment was the earliest final judgment entered on matters relevant to this proceeding," and that "the district court erred when it did not afford preclusive effect to the Texas probate court's determination of relevant legal and factual issues." *Id.* at 65.

The court of appeals rejected petitioner's argument that the earliest final judgment in the case had in fact been issued by the bankruptcy court rather than by the probate court. In the court of appeals' view, the bankruptcy court had lacked jurisdiction to enter final judg-

ment on petitioner's counterclaim. Pet. App. 55-56. The court of appeals agreed with petitioner "that her claim is a compulsory counterclaim because the 'operative facts underlying her action' are the same as those underlying [respondent's] defamation claim." *Id.* at 47 (internal quotation marks and alterations omitted). The court concluded, however, that the counterclaim was "not a 'core proceeding arising under title 11, or arising in a case under title 11' for which the bankruptcy court is empowered to enter a final judgment." *Id.* at 65 (quoting 28 U.S.C. 157(b)(1)) (brackets omitted).

The court of appeals acknowledged that 28 U.S.C. 157(b)(2)(C) defines the term "core proceedings" to include "counterclaims by the estate against persons filing claims against the estate." Pet. App. 45. The court held, however, that a bankruptcy judge may enter final judgment only on a claim "that meets Congress' definition of a core proceeding *and* arises under or arises in title 11." *Id.* at 43. In support of that conclusion, the court of appeals expressed concern that an "overly broad construction" of the term "core proceeding" would create a potential constitutional infirmity of the sort identified in *Northern Pipeline*. *Id.* at 50.

To avoid that perceived constitutional difficulty, the court of appeals adopted a test proposed in an amicus brief, under which "a counterclaim under § 157(b)(2)(C) is properly a 'core' proceeding 'arising in a case under' the Bankruptcy Code only if the counterclaim is so closely related to the proof of claim that the resolution of the counterclaim is necessary to resolve the allowance or disallowance of the claim itself." Pet. App. 50 (brackets omitted). The court concluded that petitioner's counterclaim did not satisfy that test. *Id.* at 51. The court explained that, "[e]ven if it were shown that the state-

ments made by [petitioner's] attorneys were true," petitioner would be required to make additional showings in order to prevail on her tortious-interference claim. *Ibid.* The court concluded that, because "[n]othing in [respondent's] defamation claim puts these [additional] factual and legal questions at issue," resolution of the counterclaim was not necessary to adjudicate respondent's claim against the estate, and the counterclaim therefore was not a "core proceeding" under the test the court had adopted. See *id.* at 51-55.

SUMMARY OF ARGUMENT

The court of appeals erred in placing artificial limits on the authority of bankruptcy judges to enter final judgment on counterclaims against creditors who have filed claims against the estate. The 1984 Act continued the longstanding practice of permitting a district court to refer a bankruptcy estate's counterclaim against a creditor to an adjunct for final adjudication. Congress intended to, and did, codify that practice from the Judiciary's interim rule, which in turn approximated the procedures in place under the 1898 Act. That codification was an appropriate exercise of Congress's authority to prescribe uniform laws regulating bankruptcy. Nothing in Article III prohibits Congress from permitting a district judge to place an estate's counterclaim on equal footing with a claim that the creditor himself is pressing in front of the bankruptcy judge, particularly when the counterclaim arises from the same transaction or occurrence.

A. Section 157 of Title 28 divides proceedings that a district court may refer to a bankruptcy judge into two categories: (1) "core proceedings arising under title 11, or arising in a case under title 11," and (2) proceedings

"otherwise related to a case under title 11." 28 U.S.C. 157(b)(1) and (c)(1). Bankruptcy judges may "hear and determine" (*i.e.*, enter final judgment in) the first category of proceedings, but are allowed only to "submit proposed findings of fact and conclusions of law to the district court" in the second. *Ibid.* The statute unambiguously places all "counterclaims by the estate against persons filing claims against the estate" in the first category, by including them in the statutory definition of "core proceedings." 28 U.S.C. 157(b)(2)(C).

That statutory language neither limits the types of counterclaims that may be referred for final adjudication, nor permits courts to engraft their own limits by judicial decision. By creating a subset of "core" proceedings in which a bankruptcy court may *not* enter final judgment, the court of appeals departed from the plain text of the statute, the decisions of this Court, and the Federal Rules of Bankruptcy Procedure. Congress incorporated many of the statutory examples of "core proceedings," including counterclaims, from the list of proceedings in which bankruptcy judges could enter final judgment under the Judiciary's interim rule. In enacting the 1984 Act, Congress intended to preserve rather than to reduce the scope of bankruptcy judges' authority under that rule.

B. Congress's express authorization for bankruptcy judges to enter final judgment on estate counterclaims, in accordance with the Judiciary's preexisting practice, was fully consistent with Article III. In delineating the scope of authority that bankruptcy judges may constitutionally exercise, this Court has consistently distinguished between persons who file claims against the estate and those who do not. By invoking the assistance of the bankruptcy court and seeking a portion of the res,

respondent subjected himself to the court's authority, and the court could thereafter resolve all contested issues between respondent and the estate.

The bankruptcy court's constitutional authority in this context is particularly clear with respect to *compulsory* counterclaims. A compulsory counterclaim is by definition sufficiently tied to the initial claim that principles of sound judicial administration require the two to be decided together. Allowing the bankruptcy court to adjudicate a compulsory counterclaim does not substantially expand the bankruptcy judge's authority, and a contrary rule would entail significant delay and inefficiency.

C. In responding to this Court's decision in *Northern Pipeline*, Congress enacted various measures to ensure that bankruptcy judges function as arms of the Judiciary and independent from the political Branches. Congress installed a panoply of procedural safeguards to protect bankruptcy creditors' rights when it restructured the bankruptcy courts in the 1984 Act—including appointment and removal of bankruptcy judges by the Judiciary, as well as discretionary referral of matters from the district court to the bankruptcy judge.

ARGUMENT

I. THE BANKRUPTCY CODE EXPRESSLY AUTHORIZES DISTRICT COURTS TO REFER FINAL DECISION ON ESTATE COUNTERCLAIMS TO BANKRUPTCY JUDGES.

A. The plain text of 28 U.S.C. 157 unambiguously authorizes a bankruptcy judge, pursuant to a referral by the district court, to enter final judgment on any counterclaim brought by the estate against a person who has filed a claim against the estate. Section 157(a) permits district courts to refer to bankruptcy judges "all cases

under title 11 and any or all proceedings arising under title 11 or arising in or related to a case under title 11." Section 157(b)(1) permits bankruptcy courts to "hear and determine" (*i.e.*, enter final judgment on) certain of these referred matters, including "all core proceedings arising under title 11, or arising in a case under title 11." And Section 157(b)(2)(C) defines the term "[c]ore proceedings" to include, without qualification, "counterclaims by the estate against persons filing claims against the estate."

Congress's unqualified inclusion of estate "counterclaims" in the definition of "core proceedings" identifies such counterclaims as among the matters that bankruptcy courts may finally decide under Section 157(b)(1). See *Kontrick* v. *Ryan*, 540 U.S. 443, 453 (2004) (recognizing that "in cataloging core bankruptcy proceedings" in Section 157(b)(2), "Congress authorized bankruptcy courts to adjudicate" those matters); *Granfinanciera, S.A.* v. *Nordberg*, 492 U.S. 33, 50 (1989) (recognizing that Congress "designated fraudulent conveyance actions 'core proceedings,' which bankruptcy judges may adjudicate and in which they may issue final judgments, if a district court has referred the matter to them") (citations omitted); *Marshall* v. *Marshall*, 547 U.S. 293, 303 (2006) (quoting Section 157(b)(1) and explaining that a "bankruptcy court may exercise plenary power only over 'core proceedings,'" as distinct from "noncore matters"). The plain text of the statute does not permit a court, for reasons of constitutional avoidance or otherwise, to "do[] violence" to "the facially unqualified reference to counterclaim jurisdiction" by artificially limiting its scope. *Commodities Futures Trading Comm'n* v. *Schor*, 478 U.S. 833, 842 (1985).

B. The court of appeals concluded (and respondent contends) that a bankruptcy judge's authority to enter final judgment on a particular matter depends on a "two-step approach," under which the bankruptcy court may enter judgment only on "a claim that meets Congress' definition of a core proceeding *and* arises under or arises in title 11." Pet. App. 43; see Br. in Opp. 34-35. The court's analysis assumes the existence of some "core proceedings" that do *not* "aris[e] under title 11, or aris[e] in a case under title 11." 28 U.S.C. 157(b)(1). That reading is incorrect.

"It is a fundamental canon of statutory construction that the words of a statute must be read in their context and with a view to their place in the overall statutory scheme." *Davis* v. *Michigan Dep't of Treasury*, 489 U.S. 803, 809 (1989). The 1984 Act does not direct the bankruptcy court to engage in the second step of the "two-step approach" that the court of appeals described; it establishes no standards for determining whether a particular "core proceeding" "aris[es] under title 11, or aris[es] in a case under title 11"; and it provides no guidance as to what the bankruptcy court should do if it concludes that a "core proceeding" does not satisfy that supposed independent prerequisite. In the absence of such provisions, the "two-step approach" mandated by the court below is both procedurally and substantively unworkable.

First, Section 157(b)(3) simply instructs the bankruptcy judge, "on the bankruptcy judge's own motion or on timely motion of a party," to make the binary determination "whether a proceeding [1] is a core proceeding under this subsection or [2] is a proceeding that is otherwise related to a case under title 11." 28 U.S.C. 157(b)(3); see Fed. R. Bankr. P. 7008(a), 7012(b),

9027(a)(1) and (e)(3) (requiring filings simply to state whether a proceeding is "core" or "non-core"). Neither Section 157(b)(3) nor any other provision of the statute directs the bankruptcy judge to make the further determination whether a particular "core" proceeding "aris[es] under title 11, or aris[es] in a case under title 11." Under the court of appeals' "two-step approach," however, that further inquiry is essential to the ultimate determination whether the bankruptcy judge can enter final judgment in any "core proceeding." Had Congress intended bankruptcy judges to undertake that further inquiry, it surely would have directed them to do so.

Second, the statute provides no standards for deciding whether a particular "core" proceeding "aris[es] under title 11, or aris[es] in a case under title 11." That lack of guidance stands in stark contrast with Congress's careful specification in Section 157(b)(2) of 16 different categories of "core" proceedings. To be sure, the statute's definition of "core proceeding" is not fully comprehensive, since Section 157(b)(2) states that "[c]ore proceedings include, but are not limited to," the enumerated categories. Under the court of appeals' approach, however, the Section 157(b)(2) categories will *never* resolve the question whether the bankruptcy judge can enter judgment on a particular matter. Rather, when a particular matter falls within Section 157(b)(2), the judge will *always* be required to make the further determination whether that matter "aris[es] under title 11, or aris[es] in a case under title 11"—without any statutory guidance for doing so. That requirement would largely negate Congress's effort in Section 157(b)(2) to clarify the line between those matters that the bankruptcy judge may finally adjudicate

and those on which the judge may enter only a recommended disposition.

Third, the statute nowhere describes what authority bankruptcy judges might wield over referred proceedings that are "core" but do *not* "aris[e] under title 11, or aris[e] in a case under title 11." Section 157 contains only two subsections that tell bankruptcy judges how to dispose of proceedings that are referred to them. Section 157(b)(1) authorizes bankruptcy judges to enter final judgments on "core proceedings arising under title 11, or arising in a case under title 11," while Section 157(c)(1) authorizes them to submit proposed findings and conclusions in "a proceeding that is not a core proceeding but that is otherwise related to a case under title 11." Neither of those provisions would encompass a hypothetical "core" proceeding that does *not* "aris[e] under title 11, or aris[e] in a case under title 11." Congress's failure to specify the scope of the bankruptcy judge's authority in a proceeding of that nature strongly indicates that the statute does not contemplate any such proceedings.

The only interpretation that makes sense of the entire statute, therefore, is that the term "[c]ore proceedings" in Section 157(b)(2) is simply shorthand for the "core proceedings arising under title 11, or arising in a case under title 11" that Section 157(b)(1) authorizes bankruptcy courts to "hear and determine." Under that interpretation, the above-described incongruities disappear. To determine their authority over a referred proceeding, bankruptcy judges simply determine whether the proceeding is "core" or whether the proceeding is "otherwise related to a case under title 11" (Section 157(b)(3)). If it is the former, the bankruptcy judge may enter final judgment (Section 157(b)(1)); if it is the lat-

ter, the bankruptcy judge may only submit proposed findings and conclusions to the district court (Section 157(c)(1)). Because "counterclaims by the estate against persons filing claims against the estate" are among the matters designated as "core proceedings" by Section 157(b)(2)(C), they fall within the former category, and bankruptcy judges may enter final judgment on them.

C. The process by which Section 157(b)(2)(C) was developed confirms Congress's intent to allow bankruptcy courts, pursuant to referrals from district courts, to enter final judgment on an estate's counterclaims against bankruptcy claimants. As previously discussed (see pp. 7-8, *supra*), Congress modeled Section 157 on the interim rule that the Judicial Branch had adopted in the wake of *Northern Pipeline*. See 130 Cong. Rec. at 6241-6242. That rule, like Section 157, divided proceedings referred to bankruptcy judges into two categories: proceedings in which bankruptcy judges could only submit proposed findings and conclusions, and proceedings in which they could enter final judgment. Compare Interim Bankr. R. §§ (d)(2) and (3), with 28 U.S.C. 157(b)(1) and (c)(1).

More specifically, the interim rule provided that "[i]n related proceedings the bankruptcy judge may not enter a judgment or dispositive order, but shall submit findings, conclusions, and a proposed judgment or order to the district judge, unless the parties to the proceeding consent to entry of the judgment or order by the bankruptcy judge." Interim Bankr. R. § (d)(3)(B). The interim rule stated that "[r]elated proceedings include, but are not limited to, claims brought by the estate against parties who have not filed claims against the estate"—*i.e.*, the sorts of claims that were at issue in *Northern Pipeline Const.* v. *Marathon Pipe Line Co.*,

see 458 U.S. 50, 56 (1982) (plurality opinion)—but that "[r]elated proceedings do not include" various enumerated matters. Interim Bankr. R. § (d)(3)(A). Among the matters specifically excluded from the term "related proceedings" were "counterclaims by the estate in whatever amount against persons filing claims [against] the estate." *Ibid.* With minor variations, Congress incorporated the interim rule's list of matters that were *not* "related proceedings" into the non-exhaustive list of "core proceedings" set forth in 28 U.S.C. 157(b)(2). Compare Interim Bankr. R. § (d)(3)(A), with 28 U.S.C. 157(b)(2)(A), (C), (D), (E), (G), (H), (I), (J), (L), and (N).

Nothing in the 1984 Act's text or history suggests that Congress intended to reduce the range of matters on which bankruptcy courts could enter final judgment under the interim rule. Congress had no reason to believe that the interim rule, which had been proposed and adopted by the Judiciary and had been repeatedly upheld by the courts of appeals, was inconsistent with *Northern Pipeline* or otherwise violated Article III. See 130 Cong. Rec. at 6241-6242; p. 7, *supra*. Congress's evident intent was simply to preserve the scope of bankruptcy judges' authority under the interim rule, which broadly permitted referral of counterclaims against bankruptcy claimants to bankruptcy judges for entry of final judgment.

II. DISTRICT COURTS' REFERRAL OF FINAL DECISION ON COMPULSORY COUNTERCLAIMS TO BANKRUPTCY JUDGES IS FULLY CONSISTENT WITH ARTICLE III OF THE CONSTITUTION.

This Court's precedents "demonstrate * * * that Article III does not confer on litigants an absolute right to the plenary consideration of every nature of claim by

an Article III court." *Schor*, 478 U.S. at 848. Consistent with that principle, neither the court of appeals nor respondent has suggested that a bankruptcy judge's final adjudication of a creditor's claim against a bankruptcy estate violates Article III.[1] And neither the court of appeals nor respondent has questioned the constitutional authority of the federal *district* court to decide petitioner's state-law counterclaim as part of the bankruptcy case. The narrow constitutional question presented is whether Congress, consistent with Article III, could authorize the bankruptcy judge to enter final judgment on petitioner's counterclaim (subject to appellate review as provided in 28 U.S.C. 158) rather than simply submitting proposed findings and conclusions to the district court. Congress's authorization for the bankruptcy court to enter judgment on that matter, in accordance with the Judiciary's interim-rule procedure, is consistent with this Court's precedents and with principles of sound judicial administration.

A. The court of appeals stated that a literal reading of Section 157(b)(2)(C), as encompassing all estate counterclaims against persons who have filed claims against the estate, "would certainly run afoul of the Court's holding in [*Northern Pipeline*]." Pet. App. 46. That

[1] Respondent has, however, made the narrower argument that the bankruptcy judge lacked *statutory* authority to enter final judgment on the *particular* defamation claim here, on the ground that it is a "personal injury tort" that must be tried in district court under 28 U.S.C. 157(b)(5). Br. in Opp. 42. Respondent makes a similar argument regarding petitioner's tortious-interference counterclaim. *Id.* at 43. The court of appeals did not address those issues, and they are not within the scope of the questions on which this Court granted certiorari. To the extent that respondent's arguments were preserved below, they could be considered on remand were this Court to reverse the judgment of the court of appeals.

analysis reflects a misreading of *Northern Pipeline*. In that case, the Court held that a non-Article III bankruptcy judge could not finally adjudicate a suit filed by the debtor against a defendant who had *not* filed a claim against the estate. See 458 U.S. at 56 (plurality opinion); *id.* at 87; *id.* at 89-91 (Rehnquist, J., concurring in the judgment). But neither the plurality nor the concurring Justices disputed Justice White's statement in dissent that "if Marathon had filed a claim against the bankrupt in this case, the trustee could have filed and the bankruptcy judge could have adjudicated a counterclaim seeking the relief that is involved in these cases." *Id.* at 100-101. And the Court in *Schor* subsequently observed that "a significant factor" in *Northern Pipeline* was "the absence of consent to an initial adjudication before a non-Article III tribunal." 478 U.S. at 849.

In applying the Seventh Amendment to the bankruptcy context, the Court has sharply distinguished between persons who file claims against the estate and those who do not. In *Granfinanciera*, the Court explained that, "under the Seventh Amendment, a creditor's right to a jury trial on a bankruptcy trustee's preference claim depends upon whether the creditor has submitted a claim against the estate." 492 U.S. at 58; see *Katchen* v. *Landy*, 382 U.S. 323 (1965). The Court subsequently reiterated that a claimant against the estate is not entitled to trial by jury on a voidable-preference counterclaim because "by filing a claim against a bankruptcy estate the creditor triggers the process of 'allowance and disallowance of claims,' thereby subjecting himself to the bankruptcy court's equitable power." *Langenkamp* v. *Culp*, 498 U.S. 42, 44 (1990) (per curiam) (quoting *Granfinanciera*, 492 U.S. at 58).

In two respects, the question presented here differs from the issue discussed by this Court in *Granfinanciera* and *Langenkamp*. First, respondent does not assert a Seventh Amendment right to jury trial on petitioner's counterclaim, but rather objects to final adjudication of that counterclaim by a non-Article III judge. But there is no sound reason for a different outcome in the Article III context than in the Seventh Amendment one. Indeed, the Court in *Granfinanciera* equated the two inquiries, stating that with respect to a legal cause of action, "the question whether the Seventh Amendment permits Congress to assign its adjudication to a tribunal that does not employ juries as factfinders requires the same answer as the question whether Article III allows Congress to assign adjudication of that cause of action to a non-Article III tribunal." 492 U.S. at 53.

Second, whereas *Langenkamp*, *Granfinanciera*, and *Katchen* involved voidable-preference actions, petitioner's tortious-interference counterclaim alleges a different sort of wrong. The court of appeals attached controlling weight to that distinction. Pet. App. 49. The court reasoned that, whereas the bankruptcy court in *Katchen* was required to resolve the voidable-preference issue in order to determine whether the claimant's own claim against the estate should be allowed, see *ibid.* (citing *Katchen*, 382 U.S. at 330), disposition of petitioner's counterclaim would require resolution of additional issues beyond those posed by respondent's defamation claim against the estate, see *id.* at 55. The court of appeals read *Katchen* and *Northern Pipeline* to establish a constitutional rule, which the court imported into its construction of Section 157(b)(2)(C), that a bankruptcy court may enter final judgment on an estate counterclaim "only if the counterclaim is so closely related to

the proof of claim that the resolution of the counterclaim is necessary to resolve the allowance or disallowance of the claim itself." *Id.* at 50.

The court of appeals was correct that the factual and legal overlap between claim and counterclaim was closer in *Katchen* than in this case. The *Katchen* Court's rationale for allowing bankruptcy-court adjudication of the estate's counterclaim, however, was not limited to the voidable-preference context. Rather, the Court relied on the broader rule, which it had previously applied to receivership proceedings, that "[b]y presenting their claims [the claimants against the estate] subjected themselves to all the consequences that attach to an appearance." *Katchen*, 382 U.S. at 335 (quoting *Alexander* v. *Hillman*, 296 U.S. 222, 241 (1935)). That principle, the Court explained, "is in harmony with the rule generally followed by courts of equity that having jurisdiction of the parties to controversies brought before them, they will decide all matters in dispute and decree complete relief." *Ibid.* (quoting *Alexander*, 296 U.S. at 242). Under that approach, respondent, by submitting a claim against the estate, subjected himself to the bankruptcy court's authority to resolve the estate's counterclaim, even though that process required resolution of issues beyond those implicated by respondent's defamation claim.[2]

[2] The Court in *Granfinaciera*, after quoting with approval the passage from *Katchen* discussed above, distinguished the *Katchen* Court's rationale from the "waiver" theory adopted by this Court in *Schor*. See 492 U.S. at 59 n.14. The precise nature of that distinction is unclear. It is clear, however, that respondent—like the claimant in *Katchen*, and unlike the petitioner in *Schor*—has "laid claim" to a "disputed res" to be administered in the bankruptcy proceedings. *Ibid.* *Katchen*'s reasoning is therefore fully applicable here.

As in a voidable-preference case, moreover, resolution of petitioner's counterclaim is "part of the claims-allowance process" and is "integral to the restructuring of the debtor-creditor relationship through the bankruptcy court's equity jurisdiction." *Langenkamp*, 498 U.S. at 44 (emphasis omitted). The trustee's recovery of monetary awards on estate counterclaims furthers the objectives of the Bankruptcy Code by increasing the pool of assets available to creditors. Cf. *Alexander*, 296 U.S. at 242 (observing, in the receivership context, that "[n]othing is more clearly a part of the subject matter of the main suit than recovery of all that to the *res* belongs"). To be sure, *Northern Pipeline* makes clear that the interest in maximizing the estate is not a sufficient basis for requiring a stranger to the bankruptcy to appear as a defendant before a non-Article III tribunal. But once respondent invoked the assistance of the bankruptcy court by filing his own proof of claim, the bankruptcy court was authorized to "decide all matters in dispute" between respondent and the estate and to "decree complete relief." *Katchen*, 382 U.S. at 335 (quoting *Alexander*, 296 U.S. at 242).

B. Although Section 157(b)(2)(C) applies by its terms to all "counterclaims by the estate against persons filing claims against the estate," as this case comes to the Court, the constitutional question presented involves the application of Section 157(b)(2)(C) to a *compulsory* counterclaim. The court of appeals held that the overlap between respondent's claim and petitioner's counterclaim was sufficient to make the counterclaim compul-

sory, Pet. App. 47-48, and respondent did not contest that proposition in opposing certiorari.[3]

A compulsory counterclaim, by definition, "arises out of the transaction or occurrence that is the subject matter of the opposing party's claim." Fed. R. Civ. P. 13(a)(1)(A) (incorporated in relevant part by Fed. R. Bankr. P. 7013). The Federal Rules compel a party, on penalty of forfeiture, to raise any such counterclaim in its answer to the primary claim. *Ibid.* The reason behind that rule is that the court, in adjudicating the primary claim, will be required to address that transaction or occurrence in any event. See, *e.g.*, *Southern Constr.*

[3] In light of respondent's failure to contest the matter in his brief in opposition, the Court may appropriately decide this case on the *assumption* that petitioner's counterclaim was "compulsory" within the meaning of Federal Rule of Civil Procedure 13(a). See Sup. Ct. R. 15.2. The Court should not decide whether petitioner's counterclaim is in fact compulsory, however, since that issue is outside the questions on which the Court granted certiorari, and the standards for distinguishing between compulsory and permissive counterclaims have practical importance well beyond the application and constitutionality of Section 157(b)(2)(C). Most obviously, the determination that a counterclaim is compulsory means that a defendant's failure to assert it will be treated as a forfeiture. In addition, under the Bankruptcy Code, "[a] governmental unit that has filed a proof of claim in [a bankruptcy] case is deemed to have waived sovereign immunity with respect to a claim against such governmental unit that is property of the estate and that *arose out of the same transaction or occurrence* out of which the claim of such governmental unit arose." 11 U.S.C. 106(b) (emphasis added). The italicized language closely tracks the text of Federal Rule Civil Procedure 13(a)(1)(A). An unduly broad view of the category of claims and counterclaims that "ar[i]se out of the same transaction or occurrence" might thus effectively expand the range of counterclaims that bankruptcy estates can assert against governmental bodies, in derogation of the canon that sovereign immunity waivers must be "strictly construed." *Department of the Army* v. *Blue Fox, Inc.*, 525 U.S. 255, 261 (1999) (citation omitted).

Co. v. *Pickard*, 371 U.S. 57, 60 (1962) (rule "was designed to prevent multiplicity of actions and to achieve resolution in a single lawsuit of all disputes arising out of common matters"); see also 6 Charles Alan Wright et al., *Federal Practice and Procedure* § 1409 (3d ed. 2010) (Wright).

As we explain above, *Katchen* supports the view that, if a creditor invokes the bankruptcy court's assistance by filing a claim against the estate, it thereby subjects itself to the bankruptcy court's jurisdiction over any counterclaims the estate may file. But even if the decision is read more narrowly, the square holding of the case is that, if the overlap between the initial claim and the counterclaim is sufficiently substantial, the bankruptcy judge may adjudicate the counterclaim and may enter affirmative relief against the claimant ordering him to surrender property that rightfully belongs to the estate. See *Katchen*, 382 U.S. at 335-338. While a compulsory counterclaim need not be a precise mirror image of the primary claim, the text and judicial-economic purposes of the rule dictate that a counterclaim is "compulsory" only when the allegations at the pleading stage overlap significantly enough for joint adjudication to make sense. 6 Wright §§ 1409, 1410. When a creditor invokes "the process of allowance and disallowance of claims," *Granfinanciera*, 492 U.S. at 58 (quoting *Katchen*, 382 U.S. at 336), permitting the bankruptcy court to adjudicate a compulsory counterclaim does not substantially expand the bankruptcy judge's power. By contrast, a rule requiring a claim and compulsory counterclaim to be adjudicated separately would entail significant "delay and expense" and would "dismember a

scheme which Congress has prescribed." *Katchen*, 382 U.S. at 339.[4]

C. This case is further distinguishable from *Northern Pipeline* by virtue of the substantial structural differences between the 1978 and 1984 Bankruptcy Acts. "[T]he constitutionality of a given congressional delegation of adjudicative functions to a non-Article III body must be assessed by reference to the purposes underlying the requirements of Article III"—namely, "to safeguard litigants' 'right to have claims decided before judges who are free from potential domination by other branches of government'" and "to protect 'the role of the independent judiciary within the constitutional scheme of tripartite government.'" *Schor*, 478 U.S. at 848 (quoting *United States* v. *Will*, 449 U.S. 200, 218 (1980), and *Thomas* v. *Union Carbide Agric. Prods. Co.*, 473 U.S. 568, 583 (1985). Congress's post-*Northern Pipeline* re-

[4] In *Schor*, the Court rejected an Article III challenge to the authority of the Commodities Futures Trading Commission (CFTC) to decide state-law counterclaims arising out of the same transaction or occurrence as certain federal reparations claims referred to the CFTC by statute. 478 U.S. 833. The Court recognized that such "counterclaim jurisdiction" was "necessary to make the reparations procedure workable." *Id.* at 856. It observed that it had previously upheld similar jurisdiction over state-law matters not only in *Katchen*, but also in an Article III case, *Reconstruction Fin. Corp.* v. *Bankers Trust Co.*, 318 U.S. 163, 168-171 (1943). *Schor*, 478 U.S. at 852 (explaining that, in the latter case, the Court "saw no constitutional difficulty in the initial adjudication of a state law claim by a federal agency, subject to judicial review, when that claim was ancillary to a federal law dispute"). The Court concluded "that the congressional authorization of limited CFTC jurisdiction over a narrow class of common law claims as an incident to the CFTC's primary, and unchallenged, adjudicative function does not create a substantial threat to the separation of powers." *Id.* at 854. Similar reasoning applies here.

structuring of the bankruptcy laws was consistent with both of these constitutional goals.

As to the first of those constitutional objectives, there is no "potential" for bankruptcy judges to be "dominat[ed] by other branches of government" because bankruptcy judges are insulated from both Congress and the Executive. Under the 1984 Act, bankruptcy judges are "appointed by the court of appeals of the United States for the circuit in which" their judicial district is located. 28 U.S.C. 152(a); compare *Northern Pipeline*, 458 U.S. at 53 (plurality opinion) (noting that the President appointed bankruptcy judges under the 1978 Act). They "serve as judicial officers of the United States district court established under Article III of the Constitution." 28 U.S.C. 152(a). Although there is no constitutional bar to lowering their pay, the same was true of bankruptcy referees under the 1898 Act, of whom the *Northern Pipeline* plurality observed that "the primary danger of a threat to the independence * * * came from within, rather than without, the judicial department." 458 U.S. at 80 n.31. And bankruptcy judges are removable only by the circuit judicial council, and only for cause, following a hearing. 28 U.S.C. 152(e).

As to the second goal, there is no threat to "the role of the independent judiciary within the constitutional scheme of tripartite government" because the Judiciary's employment of bankruptcy judges is entirely optional. District courts "may" refer certain bankruptcy-related matters to bankruptcy judges, but they are not required to do so. 28 U.S.C. 157(a); compare *Northern Pipeline*, 458 U.S. at 54 n.3 ("The ultimate repository of the [1978] Act's broad jurisdictional grant is the bankruptcy courts."); *id.* at 80 n.31 ("[T]he [1978] bankruptcy courts are independent of the United

States district courts.") (internal quotation marks omitted). Article III courts, moreover, exercise appellate jurisdiction over bankruptcy judges' rulings in referred matters, including de novo review of legal issues. 28 U.S.C. 157(b)(1), 158; cf. Paul Bator, *The Constitution as Architecture: Legislative and Administrative Courts Under Article III*, 65 Ind. L.J. 233, 269 (1989) ("The Constitution gives Congress wide discretion to assign the task of making the initial decision in a case arising under federal law to administrative agencies, but requires judicial review to assure the supremacy of law.").[5] And a district court always retains the authority to "withdraw, in whole or in part, any case or proceeding referred under this section, on its own motion or on timely motion of any party, for cause shown." 28 U.S.C. 157(d). Indeed, the district court in this case initially granted respondent's motion to withdraw the reference of the claim and counterclaim, before vacating the withdrawal and referring the matter back to the bankruptcy judge. See J.A. 123, 129-130.

[5] The statute itself does not prescribe a standard of review. Courts by practice review a bankruptcy judge's legal conclusions de novo, see 10 *Collier on Bankruptcy* ¶ 8013.04 (15th ed. 2010), and the current federal rules (like the 1973 rules, see p. 3, *supra*) provide that findings of fact "shall not be set aside unless clearly erroneous," Fed. R. Bankr. P. 8013. That latter standard does not violate Article III, because even in cases of private right, "there is no requirement that, in order to maintain the essential attributes of the judicial power, all determinations of fact in constitutional courts shall be made by judges." *Crowell* v. *Benson*, 285 U.S. 22, 51 (1932); see *Reconstruction Fin. Corp.*, 318 U.S. at 170 (Article III satisfied even where agency's factfinding "may not be disturbed by a court" if "supported by evidence"); see also *Dickinson* v. *Zurko*, 527 U.S. 150, 161-162 (1999) (noting that substantial-evidence review is even more deferential than clear-error review).

CONCLUSION

The judgment of the court of appeals should be vacated and the case remanded for further proceedings.

Respectfully submitted.

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NOVEMBER 2010

APPENDIX

1. 28 U.S.C. 157 provides:

Procedures

(a) Each district court may provide that any or all cases under title 11 and any or all proceedings arising under title 11 or arising in or related to a case under title 11 shall be referred to the bankruptcy judges for the district.

(b)(1) Bankruptcy judges may hear and determine all cases under title 11 and all core proceedings arising under title 11, or arising in a case under title 11, referred under subsection (a) of this section, and may enter appropriate orders and judgments, subject to review under section 158 of this title.

(2) Core proceedings include, but are not limited to—

(A) matters concerning the administration of the estate;

(B) allowance or disallowance of claims against the estate or exemptions from property of the estate, and estimation of claims or interests for the purposes of confirming a plan under chapter 11, 12, or 13 of title 11 but not the liquidation or estimation of contingent or unliquidated personal injury tort or wrongful death claims against the estate for purposes of distribution in a case under title 11;

(C) counterclaims by the estate against persons filing claims against the estate;

(D) orders in respect to obtaining credit;

(E) orders to turn over property of the estate;

(F) proceedings to determine, avoid, or recover preferences;

(G) motions to terminate, annul, or modify the automatic stay;

(H) proceedings to determine, avoid, or recover fraudulent conveyances;

(I) determinations as to the dischargeability of particular debts;

(J) objections to discharges;

(K) determinations of the validity, extent, or priority of liens;

(L) confirmations of plans;

(M) orders approving the use or lease of property, including the use of cash collateral;

(N) orders approving the sale of property other than property resulting from claims brought by the estate against persons who have not filed claims against the estate;

(O) other proceedings affecting the liquidation of the assets of the estate or the adjustment of the debtor-creditor or the equity security holder relationship, except personal injury tort or wrongful death claims; and

(P) recognition of foreign proceedings and other matters under chapter 15 of title 11.

(3) The bankruptcy judge shall determine, on the judge's own motion or on timely motion of a party,

whether a proceeding is a core proceeding under this subsection or is a proceeding that is otherwise related to a case under title 11. A determination that a proceeding is not a core proceeding shall not be made solely on the basis that its resolution may be affected by State law.

(4) Non-core proceedings under section 157(b)(2)(B) of title 28, United States Code, shall not be subject to the mandatory abstention provisions of section 1334(c)(2).

(5) The district court shall order that personal injury tort and wrongful death claims shall be tried in the district court in which the bankruptcy case is pending, or in the district court in the district in which the claim arose, as determined by the district court in which the bankruptcy case is pending.

(c)(1) A bankruptcy judge may hear a proceeding that is not a core proceeding but that is otherwise related to a case under title 11. In such proceeding, the bankruptcy judge shall submit proposed findings of fact and conclusions of law to the district court, and any final order or judgment shall be entered by the district judge after considering the bankruptcy judge's proposed findings and conclusions and after reviewing de novo those matters to which any party has timely and specifically objected.

(2) Notwithstanding the provisions of paragraph (1) of this subsection, the district court, with the consent of all the parties to the proceeding, may refer a proceeding related to a case under title 11 to a bankruptcy judge to hear and determine and to enter appropriate orders and judgments, subject to review under section 158 of this title.

(d) The district court may withdraw, in whole or in part, any case or proceeding referred under this section, on its own motion or on timely motion of any party, for cause shown. The district court shall, on timely motion of a party, so withdraw a proceeding if the court determines that resolution of the proceeding requires consideration of both title 11 and other laws of the United States regulating organizations or activities affecting interstate commerce.

(e) If the right to a jury trial applies in a proceeding that may be heard under this section by a bankruptcy judge, the bankruptcy judge may conduct the jury trial if specially designated to exercise such jurisdiction by the district court and with the express consent of all the parties.

2. The Interim Bankruptcy Court Rule of 1983 provides:

"THE RULE"

ADMINISTRATION OF BANKRUPTCY SYSTEM

(a) Emergency resolution

The purpose of this rule is to supplement existing law and rules in respect to the authority of the bankruptcy judges of this district to act in bankruptcy cases and proceedings until Congress enacts appropriate remedial legislation in response to the Supreme Court's decision in *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, — U.S. —, 102 S. Ct. 2858 (1982), or until March 31, 1984, whichever first occurs.

The judges of the district court find that exceptional circumstances exist. These circumstances include: (1) the unanticipated unconstitutionality of the grant of power to bankruptcy judges in section 241(a) of Public Law 95-598; (2) the clear intent of Congress to refer bankruptcy matters to bankruptcy judges; (3) the specialized expertise necessary to the determination of bankruptcy matters; and (4) the administrative difficulty of the district courts' assuming the existing bankruptcy caseload on short notice.

Therefore, the orderly conduct of the business of the court requires this referral of bankruptcy cases to the bankruptcy judges.

(b) Filing of bankruptcy papers

The bankruptcy court constituted by § 404 of Public Law 95-598 shall continue to be known as the United States Bankruptcy Court of this district. The Clerk of the Bankruptcy Court is hereby designated to maintain all files in bankruptcy cases and adversary proceedings. All papers in cases or proceedings arising under or related to Title eleven shall be filed with the Clerk of the Bankruptcy Court regardless of whether the case or proceeding is before a bankruptcy judge or a judge of the district court, except that a judgment by the district judge shall be filed in accordance with Rule 921 of the Bankruptcy Rules.

(c) Reference to bankruptcy judges

(1) All cases under Title eleven and all civil proceedings arising under Title eleven or arising in or related to cases under Title eleven are referred to the bankruptcy judges of this district.

(2) The reference to a bankruptcy judge may be withdrawn by the district court at any time on its own motion or on timely motion by a party. A motion for withdrawal of reference shall not stay any bankruptcy matter pending before a bankruptcy judge unless a specific stay is issued by the district court. If a reference is withdrawn, the district court may retain the entire matter, may refer part of the matter back to the bankruptcy judge, or may refer the entire matter back to the bankruptcy judge with instructions specifying the powers and functions that the bankruptcy judge may exercise. Any matter in which the reference is withdrawn shall be reassigned to a district judge in accordance with the court's usual system for assigning civil cases.

(3) Referred cases and proceedings may be transferred in whole or in part between bankruptcy judges within the district without approval of a district judge.

(d) Powers of bankruptcy judges

(1) The bankruptcy judges may perform in referred bankruptcy cases and proceedings all acts and duties necessary for the handling of those cases and proceedings except that the bankruptcy judges may not conduct:

(A) a proceeding to enjoin a court;

(B) a proceeding to punish a criminal contempt--

(i) not committed in the bankruptcy judge's actual presence; or

(ii) warranting a punishment of imprisonment;

(C) an appeal from a judgment, order, decree, or decision of a United States bankruptcy judge; or

(D) jury trials.

Those matters which may not be performed by a bankruptcy judge shall be transferred to a district judge.

(2) Except as provided in (d)(3), orders and judgments of bankruptcy judges shall be effective upon entry by the Clerk of the Bankruptcy Court, unless stayed by the bankruptcy judge or a district judge.

(3)(A) Related proceedings are those civil proceedings that, in the absence of a petition in bankruptcy, could have been brought in a district court or a state court. Related proceedings include, but are not limited to, claims brought by the estate against parties who have not filed claims against the estate. Related proceedings do not include: contested and uncontested matters concerning the administration of the estate; allowance of and objection to claims against the estate; counterclaims by the estate in whatever amount against persons filing claims the estate [*sic*]; orders in respect to obtaining credit; orders to turn over property of the estate; proceedings to set aside preferences and fraudulent conveyances; proceedings in respect to lifting of the automatic stay; proceedings to determine dischargeability of particular debts; proceedings to object to the discharge; proceedings in respect to the confirmation of plans; orders approving the sale of property where not arising from proceedings resulting from claims brought by the estate against parties who have not filed claims against the estate; and similar matters. A proceeding is not a related proceeding merely because the outcome will be affected by state law.

(B) In related proceedings the bankruptcy judge may not enter a judgment or dispositive order, but shall submit findings, conclusions, and a proposed judgment

or order to the district judge, unless the parties to the proceeding consent to entry of the judgment or order by the bankruptcy judge.

(e) District court review

(1) A notice of appeal from a final order or judgment or proposed order or judgment of a bankruptcy judge or an application for leave to appeal an interlocutory order of a bankruptcy judge, shall be filed within 10 days of the date of entry of the judgment or order or of the lodgment of the proposed judgment or order. As modified by section (e)2A and B of this rule, the procedures set forth in Part VIII of the Bankruptcy Rules apply to appeals of bankruptcy judges' judgments and orders and the procedures set forth in Bankruptcy Interim Rule 8004 apply to applications for leave to appeal interlocutory orders of bankruptcy judges. Modification by the district judge or the bankruptcy judge of time for appeal is governed by Rule 802 of the Bankruptcy Rules.

(2)(A) A district judge shall review:

(i) an order or judgment entered under paragraph (d)(2) if a timely notice of appeal has been filed or if a timely application for leave to appeal has been granted;

(ii) an order or judgment entered under paragraph (d)(2) if the bankruptcy judge certifies that circumstances require that the order or judgment be approved by a district judge, whether or not the matter was controverted before the bankruptcy judge or any notice of appeal or application for leave to appeal was filed; and

(iii) a proposed order or judgment lodged under paragraph (d)(3), whether or not any notice of appeal or application for leave to appeal has been filed.

(B) In conducting review, the district judge may hold a hearing and may receive such evidence as appropriate and may accept, reject, or modify, in whole or in part, the order or judgment of the bankruptcy judge, and need give no deference to the findings of the bankruptcy judge. At the conclusion of the review, the district judge shall enter an appropriate order or judgment.

(3) When the bankruptcy judge certifies that circumstances require immediate review by a district judge of any matter subject to review under paragraph (d)(2), the district judge shall review the matter and enter an order or judgment as soon as possible.

(4) It shall be the burden of the parties to raise the issue of whether any proceeding is a related proceeding prior to the time of the entry of the order of judgment of the district judge after review.

(f) Local rules

In proceedings before a bankruptcy judge, the local rules of the bankruptcy court shall apply. In proceedings before a judge of the district court, the local rules of the district court shall apply.

(g) Bankruptcy rules and title IV of Public Law 95-598

Courts of bankruptcy and procedure in bankruptcy shall continue to be governed by Title IV of Public Law 95-598 as amended and by the bankruptcy rules prescribed by the Supreme Court of the United States pursuant to 28 U.S.C. § 2075 and limited by SEC. 405(d) of

the Act, to the extent that such Title and Rules are not inconsistent with the holding of *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, — U.S. —, 102 S. Ct. 2858 (1982).

(h) Effective date and pending cases

This rule shall become effective December 25, 1982, and shall apply to all bankruptcy cases and proceedings not governed by the Bankruptcy Act of 1898 as amended, and filed on or after October 1, 1979. Any bankruptcy matters pending before a bankruptcy judge on December 25, 1982 shall be deemed referred to that judge.

AMICUS CURIAE BRIEF

No. 10-179

IN THE

NOV 15 2010

Supreme Court of the United States

• • •

HOWARD K. STERN, EXECUTOR OF
THE ESTATE OF VICKIE LYNN MARSHALL,
Petitioner,

—v.—

ELAINE T. MARSHALL, EXECUTRIX OF
THE ESTATE OF E. PIERCE MARSHALL,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES
COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF IN SUPPORT OF PETITIONER FOR *AMICI CURIAE* PROFESSORS RICHARD AARON, LAURA BARTELL, JAGDEEP S. BHANDARI, SUSAN BLOCK-LIEB, ROBERT D'AGOSTINO, JACKIE GARDINA, INGRID HILLINGER, GEORGE W. KUNEY, LOIS LUPICA, C. SCOTT PRYOR, KEITH SHARFMAN, MICHAEL D. SOUSA, AND ROBERT M. ZINMAN

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INTEREST OF *AMICI*[1]

The *Amici Curiae* are law professors who have devoted their careers to the teaching and study of bankruptcy law and the subject matter jurisdiction of the courts of bankruptcy.[2] They are keenly interested in this appeal because its outcome could have a significant impact on the continued efficiency of the bankruptcy courts in their handling of bankruptcy proceedings referred to them by omnibus reference orders issued by all district courts pursuant to 28 U.S.C. § 157(a). Under 28 U.S.C. § 157(b)(1), bankruptcy judges have authority, subject to control by the Article III Judiciary, to adjudicate those referred proceedings that are

[1] The *Amici* file this brief with the written consent of all parties. No counsel for a party has authored this brief in whole or in part. No person or entity, including the *Amici* or their counsel, made a monetary contribution for the preparation or submission of this brief; it has been prepared *pro bono*.

[2] The *Amici* are Richard Aaron, Professor of Law, University of Utah-S.J.Quinney College of Law; Laura Bartell, Professor of Law, Wayne State University Law School; Jagdeep S. Bhandari, Professor of Law, Florida Coastal Law School; Susan Block-Lieb, Professor of Law, Fordham Law School; Robert D'Agostino, Professor of Law, John Marshall Law School; Ingrid Hillinger, Professor of Law, Boston College School of Law; Jackie Gardina, Professor of Law, Vermont Law School; George W. Kuney, Professor of Law, University of Tennessee College of Law; Lois Lupica, Professor of Law, University of Maine School of Law; C. Scott Pryor, Regent University School of Law, Keith Sharfman, Professor of Law, St. John's University School of Law; Michael D. Sousa, Professor of Law, University of Denver-Sturm College of Law, and Robert M. Zinman, Professor of Law, St. John's University School of Law.

within the "core" category under 28 U.S.C. § 157(b)(2).

This appeal poses the question whether, in light of Article III of the Constitution, a non-Article III bankruptcy judge may be empowered to adjudicate a compulsory counterclaim of the bankruptcy trustee or debtor as a "core" proceeding against a creditor who has filed a proof of claim. It is the *Amici*'s view that in answering this question, a distinction should be made between a permissive counterclaim and one that is compulsory.[3] This is because, unlike permissive counterclaims, a compulsory counterclaim (1) must be asserted in response to the creditor's filed claim or it will be extinguished as a matter of law, and (2) is inseparably tied to the creditor's filed claim and thus must be determined as a part of the claims-allowance process for the restructuring of debtor-creditor relations, which is at the core of the federal bankruptcy power.

The *Amici* note policy concerns that if bankruptcy judges are precluded from adjudicating compulsory counterclaims, it will unduly delay the completion of bankruptcy cases and distribution to creditors while awaiting the resolution of compulsory counterclaims by the district court. It

[3] Although 28 U.S.C. § 157(b)(2)(C) literally designates both permissive and compulsory counterclaim as "core" proceedings, the question whether Article III precludes a bankruptcy judge from adjudicating permissive counterclaims is not before the Court because the Court of Appeals below found that Petitioner's counterclaim is a compulsory counterclaim. *In re Marshall*, 600 F.3d 1037, 1057 (9th Cir. 2010). This *amicus* brief does not directly address permissive counterclaims.

will also impose an unnecessary burden on district courts and cause a significant increase in the costs of bankruptcy cases. The *Amici* are also concerned that the rejection of authorization for bankruptcy judges to adjudicate compulsory counterclaims under 28 U.S.C. § 157(b)(1) and § 157(b)(2)(C), despite their integral part of a core bankruptcy function, would generate uncertainty in the lower courts regarding whether Article III precludes bankruptcy judges from determining some of the *other* proceedings that are also designated as "core" by § 157(b)(2), and could call into question the constitutionality of the entire present bankruptcy jurisdictional system.

By this *pro bono amicus* brief in support of Petitioner, the *Amici* offer their analysis of the issue to provide assistance to the Court as it considers this important question. The *Amici* believe that unique aspects of their analysis demonstrate that Article III, when interpreted and applied in light of its purposes, does not preclude a bankruptcy judge from adjudicating a compulsory counterclaim.

SUMMARY OF ARGUMENT

The Court has decided a number of cases that address whether various non-Article III systems for the adjudication of claims passed constitutional muster, and has rejected Article III challenges in most of them. Although the Court's theory for when it has upheld a non-Article system of adjudication is not evident from the case law, its jurisprudence provides insight into the circumstances under which the vesting of adjudicatory authority in a non-Article III judge does not

run afoul of Article III. What emerges as a key factor in sustaining such authority is the ability of the Article III Judiciary to control the process conducted in the non-Article III tribunal. The 1978 bankruptcy jurisdictional system before the Court in *Northern Pipeline Construction Co. v. Marathon Pipe Line Company*, 458 U.S. 50 (1982) (herein, "*Northern Pipeline*") was invalidated because the Article III Judiciary had no control whatsoever over proceedings in the bankruptcy courts. As stated by the Court, that system actually "supplant[ed] our system of adjudication in independent Art. III tribunals." *Id.* at 73. In contrast, under the present system, the Article III Judiciary has control over bankruptcy, and the Article III judges decide what proceedings will be adjudicated by a bankruptcy judge.

The constitutionality of a bankruptcy judge's authority to adjudicate compulsory counterclaims should be determined by reference to Article III's underlying objectives, particularly where, as here, any intrusion upon the Article III system of adjudication is *de minimus*. Article III's institutional and individual objectives are to ensure the independence of the Judiciary and to protect it from control of the Executive and Legislative branches. *Northern Pipeline*, 458 U.S. at 59. In light of the Article III Judiciary's control, authorization of non-Article III bankruptcy judges to adjudicate compulsory counterclaims does not stand in the way of achieving Article III's institutional objective to protect the federal Judiciary from pressure exerted by the political branches of the government.

A creditor's personal right to an Article III adjudication does not extend to claims that are an integral part of the claims-allowance process triggered by its filing of a proof of claim. Such right does not extend to compulsory counterclaims, which must be adjudicated on the merits and their damages assessed to determine the fate of the creditor's claim, and in turn, all of the creditors' claims, in order to allocate the property of the estate for distribution to creditors. *Tennessee Student Assistance Corp. v. Hood*, 541 U.S. 440, 448 (2004). The bankruptcy courts' *in rem* jurisdiction thus encompasses the determination of compulsory counterclaims. The authorization of non-Article III bankruptcy judges to adjudicate claims that directly involve the bankruptcy *res* implements the bankruptcy function of distribution of estate assets to creditors, and does not stand in the way of accomplishing the objectives of Article III.

The determination of compulsory counterclaims is an essential part of "the restructuring of debtor-creditor relations, which is at the core of the federal bankruptcy power." *Northern Pipeline*, 458 U.S. at 71 (plurality); 458 U.S. at 95 (dissent); *See also Langenkamp v. Culp*, 492 U.S. 42, 44 (1990). The universe of claims against the bankruptcy estate must be fully determined in order to restructure debtor-creditor relations, and the total amount of allowed claims cannot be known without adjudicating compulsory counterclaims. Such counterclaims are forced into the bankruptcy case and become creatures of bankruptcy as an integral part of the debtor-creditor restructuring process. The bankruptcy judges' authority to adjudicate compulsory counterclaims should be upheld

because they are at the core of the federal bankruptcy power.

The system that has been established for bankruptcy is predicated on the fundamental principle that the bankruptcy court is a court of equity and "applies the principles and rules of equity jurisprudence." *Young v. United States*, 535 U.S. 43, 50 (2002) (quoting *Pepper v. Litton*, 308 U.S. 295, 304 (1939)). Under principles of equity jurisprudence, the equity power extends to all parts of the dispute between the parties that arise from the same operative facts. Thus, equity does not require parties to litigate one part of a controversy in one court, and another part in a different court. Under this principle of equity, Article III does not preclude non-Article III judges from determining compulsory counterclaims as part of the equitable claims-allowance process.

A right to an Article III adjudication should not fare any better than other constitutional rights that are lost because of the filing of a proof of claim. Creditors who have filed proofs of claim thereby lose various constitutional rights regarding determinations to be made within the equitable claims-allowance process. For example, a creditor who files a proof of claim forfeits a Seventh Amendment right to trial of the claim by a jury. Likewise, by filing a proof of claim, a State foregoes its Eleventh Amendment right not to be required to litigate in a federal court in order to establish its claim. Similarly, by filing a proof of claim, the creditor should be held to forego an Article III objection to the bankruptcy judge's authority to adjudicate a compulsory counterclaim.

A compulsory counterclaim must be adjudicated on its merits and the damages it seeks must be liquidated in order to know the outcome of the creditor's claim. It makes no sense for the parties to try the merits of a compulsory counterclaim and its damages before a bankruptcy judge, and then to require the counterclaiming party to bring another proceeding in district court to obtain a money judgment.

ARGUMENT

POINT I

THE AUTHORITY OF NON-ARTICLE III BANKRUPTCY JUDGES TO HEAR COMPULSORY COUNTERCLAIMS IS NOT PRECLUDED BY ARTICLE III IN LIGHT OF THE ARTICLE III JUDICIARY'S CONTROL OVER BANKRUPTCY

A. Under the Court's Jurisprudence, Control of Litigation in the Non-Article III Court by the Article III Judiciary Emerges as a Key Factor Supporting a Non-Article III Adjudication of Compulsory Counterclaims

Article III of the Constitution provides that the federal judicial power shall be exercised by life-tenured judges whose compensation is protected from reduction. However, the Court has held that in some circumstances, Congress may authorize various persons who lack Article III attributes to adjudicate the rights of the parties. During the 1800s, the Court established exceptions to Article III for territorial courts, military tribunals, and

so-called "public rights" cases.[4] In five more recent cases, the Court considered the constitutionality of various non-Article III systems for the adjudication of controversies. The Court upheld such systems in four cases: *Crowell v. Benson*, 285 U.S. 22 (1932); *United States v. Raddatz*, 447 U.S. 667 (1980); *Thomas v. Union Carbide Agric. Prods. Co.*, 473 U.S. 568 (1985); *Commodity Futures Trading Comm'n v. Schor*, 478 U.S. 833 (1986) (herein, "*Schor*"). In the fifth case, *Northern Pipeline*, the Court ruled that the system at issue violated Article III. However, the circumstances in which a non-Article III adjudication will pass constitutional muster are not altogether clear from the case law.

In *Northern Pipeline*, the Court illuminated the issue in the bankruptcy context. There, the Court invalidated the 1978 bankruptcy system, holding that Article III barred a non-Article III bankruptcy court from adjudicating a debtor's contract claim against a defendant who had not filed a proof of claim against the bankruptcy estate. The present jurisdictional structure, enacted in 1984, is materially different from the one invalidated by *Northern Pipeline*. Whereas the present system provides the Article III Judiciary with control over bankruptcy, the 1978 scheme violated Article III because it vested no control whatsoever in the Article III Judiciary. As explained by the Court, the problem with the 1978 system was that it "supplant[ed] completely our system of adjudication in independent Art. III tribunals," and "provide[d] no limiting principle." *Id.* at 73. By

[4] These early exceptions to Article III are discussed in *Northern Pipeline*, 458 U.S. at 64-68

contrast, the present system vests control over the bankruptcy courts in the Article III Judiciary. Bankruptcy judges are appointed by the courts of appeals, and constitute units of the district court. 28 U.S.C. §§ 151 and 152(a)(1). Moreover, the district courts are empowered to decide, in their discretion, what proceedings they will send to the bankruptcy judges. Further, at any time, the district courts may withdraw the reference of any, or even all, of the proceedings previously referred to a bankruptcy judge, for adjudication by the district court itself. 28 U.S.C. §§ 151, 152 and 157(d). The Article III Judiciary thus decides who will be the bankruptcy judges, what proceedings will be sent to them, and which ones they will retain. Control by the Article III Judiciary of the adjunct bankruptcy judges is a key factor among those which, under the Court's jurisprudence, support the authorization of bankruptcy judges to adjudicate compulsory counterclaims. The present system for bankruptcy should be upheld because it is structured on control of the system by the Article III Judiciary.

Article III should be interpreted and applied in light of its objectives, and the resolution of an Article III challenge "cannot turn on conclusory reference to the language of Article III." *Schor*, 478 U.S. at 847. The primary objective of Article III is to protect the federal Judiciary from incursion by the Legislative and Executive branches of the federal government. *Northern Pipeline*, 458 U.S. at 59; *Schor*, 478 U.S. at 848. That objective is not impaired by the adjudication of compulsory counterclaims by non-Article III bankruptcy judges, and granting such authorization to non-

Article III bankruptcy judges is "consistent with, rather than threatening to, the constitutional mandate of separation of powers." *Northern Pipeline*, 458 U.S. at 64.

Not only does authorizing bankruptcy judges to adjudicate compulsory counterclaims not impair Article III's purpose, but moreover, the adjudication of compulsory counterclaims is an integral part of the equitable claims-allowance process, which is an essential part of the bankruptcy system. *Langenkamp*, 498 U.S. at 44. Compulsory counterclaims asserted against a proof of claim must be adjudicated and their damages assessed in order to determine the allowance of the creditor's claim. The process must be completed so that the universe of allowed claims against the bankruptcy estate will be known. That information is essential to restructure debtor-creditor relations, which is at the core of the federal bankruptcy power. The bankruptcy system operates under the control of the Article III Judiciary, and such control protects the system from incursions by the political branches. The adjudication of compulsory counterclaims by bankruptcy judges thus does not run afoul of Article III.

In the Bankruptcy Amendments and Federal Judgeship Act of 1984, by which the present system was enacted, Congress created the jurisdictional system that replaced the one held unconstitutional under Article III in *Northern Pipeline*. There the Court held that the 1978 scheme ran afoul of Article III because it totally supplanted the system of adjudication in independent Article III courts. In response to this ruling, the 1984 Amendments, which continue in

effect, vested bankruptcy jurisdiction in the district courts and authorized them to assign bankruptcy proceedings to the bankruptcy judges, and further authorized the district courts to take back from the bankruptcy judges any or all proceedings at any stage, for adjudication by the district court itself. By this means, the bankruptcy courts operate within the present system under the control of the Article III Judiciary. This is because the district courts decide whether to refer bankruptcy proceedings and whether to withdraw the reference so as to take them back for an Article III court's determination. The key factor supporting the constitutionality of the authorization to bankruptcy judges to adjudicate compulsory counterclaims is the control vested in the Article III Judiciary.

B. The Article III Judiciary's Control Over the Bankruptcy Courts Prevents Encroachment on the Independence of the Article III Judiciary, Thereby Satisfying the Institutional Purpose of Article III

Article III, § 1, of the Constitution protects the independence of the federal Judiciary from encroachment or aggrandizement by the Legislative and Executive branches of the government. While a system under which non-Article III judges have some adjudicatory authority must, for the most part, leave the "essential attributes of judicial power" in Article III courts, *Schor*, 478 U.S. at 852, the Court has recognized that Article III does not bar Congress from acting under Article I to vest some decision-making authority in non-Article III courts and federal agencies. *See, e.g., Schor*, 478 U.S. at 852; *Waters v. National Assn. of Radi-*

ation Survivors, 473 U.S. 305 (1985); *Palmore v. United States*, 411 U.S. 389 (1973); *Crowell v. Benson*, 285 U.S. 22 (1932); *Murray's Lessee v. Hoboken Land & Improvement*, 18 How. 272 (1856).

Under various circumstances, the Court has upheld authorizations of non-Article III courts and agencies to make final adjudications. The plurality in *Northern Pipeline* endorsed the proposition that non-Article III tribunals could finally adjudicate particular matters without running afoul of Article III, specifically reaffirming the holding of *Crowell*, "that Congress may assign to non-Article III bodies some adjudicatory functions." *Northern Pipeline*, 458 U.S. at 80 n.32. Moreover, the plurality reaffirmed the constitutionality of the magistrate system, which was upheld in the face of an Article III challenge in *Raddatz*. *See id.* at 81. The Court's holding in *Northern Pipeline* is quite narrow, concluding that a debtor's contract action against a defendant who did not file a proof of claim could not constitutionally be adjudicated by a non-Article III judge. The critical element in *Northern Pipeline*, which differs from this case, was that the 1978 bankruptcy jurisdictional system granted unlimited adjudicatory authority to the non-Article III bankruptcy judges under a system that provided no control whatsoever for the Article III Judiciary. *Northern Pipeline*, 458 U.S. at 85. Under the 1978 system, Congress enabled the non-Article III bankruptcy courts to exercise "all powers of law, equity and admiralty." *Id.* at 55. Moreover, although the 1978 statute nominally vested bankruptcy jurisdiction in the district courts, that statute automatically empowered the

non-Article III bankruptcy judges, who were Presidential appointees, to exercise complete jurisdiction over all bankruptcy proceedings without any control or supervision whatsoever by the Article III Judiciary. As observed by the Court, all powers of an Article III court were given to the non-Article III bankruptcy judges, hidden "behind the façade of a grant to the district courts." *Id.* at 86.

The Court has upheld the constitutionality of numerous provisions authorizing non-Article III judges and administrative agencies to adjudicate controversies. In assessing whether a particular delegation of adjudicative power encroaches on the independence of the Article III Judiciary, this Court has been "guided by the practical effects of [a] congressional action rather than 'formalistic and unbending rules.'" *See Northern Pipeline*, 458 U.S. at 81; *see also Schor*, 478 U.S. at 581; *Thomas*, 473 U.S. at 587. As stated by the Court:

> Great constitutional provisions must be administered with caution. Some play must be allowed for the joints of the machine and it must be remembered that legislatures are ultimate guardians of the liberties and welfare of the people in quite as great a degree as the courts.

Mo., Kans. & Tex. Ry. Co. of Tex. v. May, 194 U.S. 267, 270 (1904) (Holmes, J.).

The Court's jurisprudence has focused on "substance rather than doctrinal reliance on formal categories" when considering Article III challenges. *Schor*, 478 U.S. at 848. When there are safeguards in place to ensure that the independence of the Article III Judiciary is not threat-

ened, the Court has upheld the grant of adjudicative authority to non-Article III judges and agencies. The Court has done so in at least seven of its decisions over the past 150 years. The 1978 bankruptcy jurisdictional system is the only one the Court held to have run afoul of Article III—and that because it *entirely* replaced the Article III courts with non-Article III bankruptcy judges without any protection whatsoever from pressures exerted by the political branches.

The Court has rejected Article III challenges to non-Article III adjudications—five times before *Northern Pipeline* and twice since—thus recognizing that non-Article III tribunals may enter final judgments without offending Article III. *E.g.*, *Schor* 478 U.S 833; *Thomas*, 473 U.S. 568. In *Schor*, the Court held that allowing an administrative agency jurisdiction over state law counterclaims was not a violation of Article III. *Schor*, 478 U.S. at 857. Expressly rejecting a "slippery slope" argument, the *Schor* Court affirmed that Congress may constitutionally delegate decision-making authority to non-Article III tribunals when that delegation does not shift the "essential attributes of judicial power" to non-Article III courts to such extent that the system "impermissibly intrude[s] on the province of the judiciary." *Schor*, 478 U.S. at 851-852. To comport with Article III values, the independence of the Judiciary must be protected. The controls held by the Article III Judiciary under the present system provide that protection.

The importance of control is evident from *Northern Pipeline*'s rejection of the contention that the 1978 system was analogous to the earlier

bankruptcy referee system, because under the earlier system the referees were under the control of the district courts. In *Northern Pipeline*, the Court focused on the fact that under the 1978 structure, which replaced the referee system, the district court did not have any control whatsoever over the bankruptcy jurisdictional system. Under the pre-1978 system, the bankruptcy referee's power was derived solely from the district courts. The district courts appointed the referees, who served at the pleasure of the district courts, and the referees only heard matters at the discretion of the district court. The Article III judges' control over referees insulated the system from interference by the political branches of government, a protection that the 1978 system lacked, but which is once again provided by the present system. *Northern Pipeline*, 458 U.S. at 79 n.31.

Two years after *Northern Pipeline*, Congress enacted the Bankruptcy Amendments and Federal Judgeship Act of 1984. This was an effort to "cure the constitutional defect" in the 1978 system. *In re Arnold Print Works, Inc.*, 815 F.2d 165, 166-167 (1st Cir. 1987) (Breyer, J.). The 1984 amendments completely overhauled the bankruptcy jurisdiction scheme, giving the Article III Judiciary the control over bankruptcy courts that it lacked under the 1978 system. Under 28 U.S.C. § 157(a), bankruptcy judges have the authority, subject to control by the district courts, to adjudicate only those proceedings that have been referred to them by the district courts. Pursuant to 28 U.S.C. § 157(d), the district court has the authority to withdraw for cause any or all proceedings that have been so referred. Further, the 1984 Amend-

ments shifted the power to appoint bankruptcy judges from the Executive branch to the courts of appeals. 28 U.S.C. § 152(a)(1). The courts of appeals also decide whether to reappoint bankruptcy judges at the end of their 14-year term, and the judicial council of the circuit, composed of Article III judges, is empowered to remove them. 28 U.S.C. §§ 152(e) and 332. Therefore, the Article III Judiciary decides who will sit on the bankruptcy bench, what proceedings will be referred to the bankruptcy courts, and what proceedings the bankruptcy judges will retain. This control over the bankruptcy system insulates the bankruptcy judges from any attempts by the Legislative or Executive branches to exert influence over them.

The authority of the district court to withdraw any or all proceedings that have been referred to the bankruptcy judges is an especially important means for the Article III Judiciary to deal with efforts from outside the Judiciary to exercise control over bankruptcy judges. The power to decide which proceedings the bankruptcy judges will retain serves to protect bankruptcy judges from outside influence. If a district court has any concern about external interference, it has the authority to withdraw the reference *sua sponte*. 28 U.S.C. § 157(d). In 2008, district courts withdrew 429 proceedings from the bankruptcy courts; in 2009, they withdrew 407.[5]

District courts have exercised their control in significant ways. For example, after the District

[5] United States Courts, Statistics: Judicial Business of the U.S. Courts 2009 (2009), http://www.uscourts.gov/Statistics/JudicialBusiness/JudicialBusiness2009.aspx (follow link at C2, page 2)

Court for the District of Delaware referred all bankruptcy proceedings to the bankruptcy judge of the district by its 1984 order, the District Court withdrew the bankruptcy court's *entire* caseload by an order entered in January 1997, which authorized the Chief Judge of the District Court to assign the particular bankruptcy proceedings to any of the several district judges or the bankruptcy judge. That order remained in effect until October 2001, when the District Court reinstated its previous automatic reference of all proceedings to the bankruptcy judges.[6] In the District of Delaware, therefore, for a period of almost five years, the Chief District Judge exercised discretion to select what proceedings would be retained in the district court or sent to the bankruptcy judge.

C. The Bankruptcy Courts' Ability to Adjudicate Compulsory Counterclaims, a Limited Class, Provides "a Limiting Principle" to the Bankruptcy Courts' Authority and Ensures that the Intrusion Upon the Article III Judiciary is *De Minimis*

The bankruptcy courts are not authorized under the present system to adjudicate claims of the *Northern Pipeline* type, and their full adjudicatory

[6] Order of Jan. 23, 1997, In re Referral of Title 11 Proceedings to The United States Bankruptcy Judges For This District, District of Delaware, available at http //www.ded.uscourts.gov/StandingOrdersMain.htm (bottom of page) (withdrawing the automatic reference); *see also*, the website for the District Court of Delaware, http://www.ded.uscourts.gov/StandingOrdersMain.htm (bottom of page) (listing orders establishing, withdrawing and reinstating the reference of cases under title 11 to the bankrutpcy judges in Delaware).

authority is limited to claims that are central to bankruptcy and its process. 28 U.S.C. § 157(b)(1) and (2). In this case, the *Amici* only suggest that the Court uphold the bankruptcy courts' authority to determine a limited class of claims—compulsory counterclaims—which would be extinguished if not asserted in response to a creditor's proof of claim. Allowing the bankruptcy courts to determine this limited class of claims does not pose a danger that the other branches of the government will be able to intrude on the independence of the Judiciary.

In *Schor*, the Court upheld the authority given to a federal agency to adjudicate a broker's counterclaim to recover an account debit where the counterclaim arose out of the same operative facts as its customer's claim, and the scope of the counterclaim thus was limited. *Schor*, 478 U.S. at 854-857. The Court explained:

> It . . . bears emphasis that the CFTC's assertion of counterclaim jurisdiction is limited to that which is necessary to make the reparations procedure workable. The CFTC adjudication of common law counterclaims is incidental to, and completely dependant upon, adjudication of reparations claims created by federal law, and in actual fact is limited to claims arising out of the same transaction or occurrence as the reparations claims.
>
> In such circumstances, the magnitude of any intrusions of the Judicial Branch can only be termed *de minimis*.

Id. at 856.

Each of the elements present in *Schor* that sustained the counterclaim jurisdiction from an Article III challenge in that case are satisfied in the present case:

First: The counterclaim jurisdiction conferred on the bankruptcy judges is *limited*, and is *necessary* to make the claims-allowance process *workable*.

Second: The adjudication of the creditor's proof of claim is *completely dependant upon* adjudication of the compulsory counterclaim because a compulsory counterclaim must be adjudicated in order to determine whether to allow the creditor's claim.

Third: A compulsory counterclaim arises out of the *same operative facts* as the creditor's proof of claim, and must be asserted in a bankruptcy case in response to a proof of claim because of *federal* law. Fed. R Bankr. P. 7013.

Fourth: To the extent, if any, that such authorization makes any intrusion on Article III, the limitation to compulsory counterclaims makes such intrusion *de minimus*.

When measured by (a) Article III's objectives, (b) the Article III Judiciary's control over what proceedings a bankruptcy judge may adjudicate, (c) the importance of a workable and efficient bankruptcy system, (d) the enormously heavy workload of the district courts, and (e) the limited intrusion on Article III, that Article should not be interpreted to preclude bankruptcy judges from adjudicating compulsory counterclaims and entering money judgments thereon.

POINT II

A CREDITOR WHO HAS FILED A PROOF OF CLAIM DOES NOT HAVE A RIGHT TO AN ARTICLE III DETERMINATION OF A COMPULSORY COUNTERCLAIM

A. The determination of Compulsory Counterclaims as Part of the Claims-Allowance Process Lies at the Core of the Federal Bankruptcy Power

The Court has recognized that the determination of creditors' claims in the claims-allowance process is fundamental to the restructuring of the debtor-creditor relationship, *Langenkamp*, 498 U.S. at 44 (citing *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33, at 57-58 (1989)), and therefore lies at the very core of the federal bankruptcy power, *Northern Pipeline*, 458 U.S. at 71 (plurality opinion). It has also recognized that whether *federal* rights are involved is significant to the Article III issue. In this case, not only is the federal bankruptcy power involved, but because a proof of claim was filed, federal law is also the source of the obligation to interpose the compulsory counterclaim. Fed. R. Bankr. P. 7013; *Cf. Northern Pipeline*, 458 U.S. at 84.

When a debtor files for bankruptcy, any creditor seeking to share in a distribution from the bankruptcy estate must file a proof of claim. 11 U.S.C. § 501. Merely filing a proof of claim, however, does not entitle the creditor to allowance of that claim; rather, by filing a proof of claim the creditor initiates a *process*, which ultimately

results in the bankruptcy court's determination of the allowability and amount (if any) of the creditor's claim. 11 U.S.C. § 502. The Court has consistently recognized that bankruptcy jurisdiction's nature is *in rem*, *Gardner v. New Jersey*, 329 U.S. 565, 574 (1947)); *Tenn. Student Assistance Corp. v. Hood*, 541 U.S. at 447-48, and that the claims-allowance process lies at the core of the federal bankruptcy power, *Northern Pipeline*, 458 U.S. at 71.

Because claims allowance is a single, unitary process, the adjudication of a creditor's claim necessarily requires determination of all issues bearing upon the validity and amount of the claim—including any defenses thereto. 11 U.S.C. §§ 502(b), 502(d), and 558. One such defense is a compulsory counterclaim, which is a claim that arises out of the same transaction or occurrence as the creditor's claim against the bankruptcy estate. Fed. R. Bankr. P. 7013. Without determining the merits and liquidating the amount of a compulsory counterclaim, the bankruptcy court cannot adjudicate the creditor's net claim.

Thus, under the present jurisdictional scheme, if the claims-allowance process is to be conducted and completed efficiently, bankruptcy judges must have authority to adjudicate compulsory counterclaims. Bifurcating the claims-allowance process into one class of affirmative creditor claims and another class of responsive compulsory counterclaims—which would be tried in different fora —would create a false dichotomy undermining a well-settled primary function of bankruptcy courts, and running counter to the equitable nature of the claims-allowance process.

B. Once a Creditor has Filed a Proof of Claim, a Compulsory Counterclaim Filed by the Bankruptcy Trustee or Debtor Becomes an Inseparable Element of the Claims-Allowance Process Triggered by the Creditor's Filing a Proof of Claim

Any creditor seeking an equitable distribution from the *res* of the bankruptcy estate must file a proof of claim in the case. 11 U.S.C. § 501. The bankruptcy court may allow claims in one of three ways: (1) claims to which no objections are filed are deemed allowed, 11 U.S.C. § 502(a); (2) the court may allow a claim over a filed objection, 11 U.S.C. § 502(b); or (3) the court may estimate a claim, 11 U.S.C. § 502(c). Where a party objects to a filed proof of claim, all issues bearing upon the allowability of the claim must be determined. 11 U.S.C. § 502(b).

Once faced with a given claim, the bankruptcy trustee or debtor may responsively assert any defenses that the debtor otherwise could have asserted. 11 U.S.C. §§ 502(b), 502(d), and 558; Fed. R. Bankr. P.7013. To the extent a defense is sustained, it operates to reduce or negate the creditor's claim. Further, § 502(b)(1) stipulates that a creditor's claim is disallowed to the extent that the claim is unenforceable against the debtor or its property. 11 U.S.C. § 502(b)(1). In other words, the bankruptcy court *must* first adjudicate the merits of any defenses to a claim before determining the allowance or disallowance of that claim.

One such defense—which *must* be heard and determined as a condition precedent to adjudication of that creditor's net claim—is the compulsory

counterclaim. A compulsory counterclaim is a counterclaim that: (1) arises out of the same transaction or occurrence as the claim to which it responds; and (2) does not require joinder of parties over which the court cannot acquire jurisdiction. Fed. R. Bankr. P. 7013. Where a litigant fails to assert a compulsory counterclaim, that claim is barred permanently. *See, e.g.*, Charles Alan Wright et al., 6 Fed. Prac. & Proc. Civ. § 1401 (3d ed.) (citing *Baker v. Gold Seal Liquors, Inc.*, 417 U.S. 467, 469 n.1 (1974).

As the Court has explained, "[i]t is traditional bankruptcy law that he who invokes the aid of the bankruptcy court by offering a proof of claim and demanding its allowance must abide the consequences of that procedure." *Gardner v. New Jersey*, 329 U.S. at 573 (citing *Wiswall v. Campbell*, 93 U.S. 347, 351 (1876)). Because a creditor's filing *forces* the bankruptcy trustee or debtor to interpose a compulsory counterclaim, the "restructuring of debtor-creditor relations, which is at the core of the federal bankruptcy power," *Northern Pipeline*, 458 U.S. at 71, requires the bankruptcy court to determine that counterclaim.

Viewed structurally, then, claims allowance is a single, unitary process. An argument to the contrary is necessarily an argument that bankruptcy courts should not retain control over the claims-allowance process, and that claims allowance can be conducted only in an Article III court.

The fact that the *creditor's* affirmative act of filing a claim triggers the compulsory counterclaim —*i.e.*, the *creditor* puts the compulsory counterclaim at issue in the restructuring of the debtor-creditor relationship—carries important

consequences. The Court has drawn a "clear distinction" between cases where a creditor has filed a proof of claim and cases where a party with no connection to the bankruptcy case finds itself pulled unexpectedly into bankruptcy court. *Langenkamp*, 498 U.S. at 44. Specifically, a creditor that files a proof of claim subjects itself to the bankruptcy court's equitable jurisdiction. *Id.* (citing *Granfinanciera*, 492 U.S. at 57–58). Accordingly, such creditor should not be heard to complain that while the bankruptcy court has authority to determine the creditor's claim, that same court somehow lacks authority over the compulsory counterclaim. Thus, "to the extent that Article III reflects a concern for procedural fairness," *In re Arnold Print Works, Inc.*, 815 F.2d at 170 (Breyer, J.) (internal citation omitted), such creditor—having triggered bankruptcy court jurisdiction by filing its proof of claim—cannot be heard to complain of any unfair surprise when the bankruptcy court determines a compulsory counterclaim. *See also, Gardner v. New Jersey*, 329 U.S. at 573-574 (by filing a proof of claim, a State cannot complain that the process for adjudicating its claim constitutes a federal suit against it in violation of its Eleventh Amendment rights).

C. Preventing Bankruptcy Judges from Determining Compulsory Counterclaims to Proofs of Claim Would Undermine the Well-Settled, Equitable Nature of the Claims-Allowance Process

It is a fundamental tenet of the Court's bankruptcy jurisprudence that bankruptcy courts are courts of equity, which "appl[y] the principles and rules of equity jurisprudence." *Young v.*

United States, 535 U.S. at 50 (citing *Pepper v. Litton*, 308 U.S. 304). The Court has specifically recognized that the claims-allowance process is an equitable proceeding. *E.g. Katchen v. Landy*, 382 U.S. 323, 335 (1966) (citing *Alexander v. Hillman*, 296 U.S. 222, 241 (1935). In determining the parameters of such an equitable proceeding, the Court has consistently looked to the historical powers of courts of equity. *E.g., Grupo Mexicano de Desarrollo v. Alliance Bond Fund, Inc.*, 527 U.S. 308, 318 (1999) (citing *Atlas Life Ins. Co. v. W.I. Southern, Inc.*, 306 U.S. 563 (1939)) (equity jurisdiction is "an authority to administer in equity suits the principles of the system of judicial remedies which had been devised and was being administered by the English Court of Chancery at the time of the separation of the two countries.").

Historically, the powers of equity courts were broad and flexible, and evolved as a counterpoint to the rigid strictures of the common law pleading rules in the law courts. For example, a litigant desirous of pre-trial discovery in connection with a claim at law had to submit the controversy to the equity court because that was the only forum where discovery was available. *See* Story, Commentaries on Equity Jurisprudence, § 64k, at 70 (1st ed. 1836). Significantly, once a litigant thus invoked the equity court's jurisdiction for discovery, the court sitting in equity would adjudicate the entire dispute—including the claim that would otherwise be triable only at law. *See* Story, Commentaries on Equity Jurisprudence § 71, at 75-76 (1st ed. 1836); *Russell v. Clarke's Executors*, 7 Cranch. 69, 91 (1812) (After granting discovery, an equity court "will proceed to determine the whole matter in controversy"). The rationale was

to establish "a convenient and uniform principle of jurisdiction . . . that where [equity] jurisdiction once attaches for discovery, and the discovery is actually obtained, the [equity] court will further entertain the bill for relief, if the plaintiff prays it." Story, Commentaries on Equity Jurisprudence § 71, at 75.

Notably, the modern compulsory counterclaim rule is a direct descendant of the equitable doctrine of recoupment. *See, e.g.*, Charles Alan Wright et al., 6 Fed. Prac. & Proc. Civ. § 1401 (3d ed.) (citing Theodore Sedgwick, 3 Theory of Damages § 1042 (9th ed. 1912); Joseph Story, Commentaries on Equity Jurisprudence § 1878 (14th ed. 1918). Historically, courts have treated recoupment not as a separate counterclaim, but rather as an indivisible subpart of the same, unitary claim that the plaintiff initially filed, because their underlying operative facts were the same. *Id.* More recently, the Court has done the same. *See, e.g.*, *Stone v. White*, 301 U.S. 532, 539 (1937) (equitable recoupment "inheres in [plaintiff's] cause of action") (internal citation omitted).

Thus, a compulsory counterclaim—viewed in light of its historical antecedent, equitable recoupment—is an inseparable component of adjudicating the creditor's claim. Consequently, the bankruptcy court's equitable power over the creditor's claim necessarily includes authority over a compulsory counterclaim.

Furthermore, once a bankruptcy court has reached the merits of a compulsory counterclaim and necessarily begun liquidating damages, there is no sound reason for denying it authority to enter judgment for the damages in excess of the

claim—even though the result is a net recovery *against the creditor*. Referring to *Katchen v. Landy*, which concerned a preference action asserted defensively against a creditor's claim, the Court has stated that, "once a creditor has filed a claim against the estate, the bankruptcy trustee may recover the full amount of any preference received by the creditor-claimant, even if that amount exceeds the amount of the creditor's claim." *Granfinanciera*, 492 U.S. at 59 n.14 (citing *Katchen v. Landy*, 382 U.S. at 337–38). The Court's equity jurisprudence thus supports authorizing bankruptcy judges to determine compulsory counterclaims, even where the value of the counterclaim exceeds the value of the creditor's claim.

D. The Court's Bankruptcy Jurisprudence Since *Northern Pipeline* Supports the Proposition that Bankruptcy Judges May Adjudicate Compulsory Counterclaims to Filed Proofs of Claim

There is a distinction of constitutional significance between proceedings against a person with no independent connection to the bankruptcy, and a claim that a trustee or debtor must assert against a creditor that filed a proof of claim. In *Granfinanciera*, a party entirely unconnected to the bankruptcy case found itself sued in bankruptcy court for a fraudulent transfer. The Court addressed whether that party retained its constitutional right to a jury trial. *Granfinanciera*, 492 U.S. at 36. In holding that it did, the Court explained that because the defendant had not filed a proof of claim—and therefore had not triggered the bankruptcy court's equitable jurisdiction—the proceeding remained one at law, and the defen-

dant thus retained its jury-trial right. *Granfinanciera*, 492 U.S. at 57-59.

One year later, in *Langenkamp v. Culp*, the Court faced a different question: whether a creditor that *had* filed a proof of claim retained a jury-trial right in a preference action filed by the debtor. *Langenkamp*, 492 U.S. at 42-43. The Court explained that the creditor did *not* have a right to a jury trial precisely because it *had* filed a proof of claim—thus, the subsequent preference action became part of the claims-allowance process. *Langenkamp*, 492 U.S. at 45. As the Court explained, "the creditor's claim and the ensuing preference action by the trustee become integral to the restructuring of the debtor-creditor relationship through the bankruptcy court's equity jurisdiction." *Langenkamp*, 492 U.S. at 45 (citing *Granfinanciera v. Nordberg*, 492 U.S. at 57-58).

A compulsory counterclaim is drawn into a bankruptcy proceeding only because a creditor has first triggered the bankruptcy court's equitable jurisdiction by filing a proof of claim. Thus, like the preference claim in *Langenkamp*, the creditor's claim and the ensuing compulsory counterclaim by the bankruptcy estate "become integral to the restructuring of the debtor-creditor relationship through the bankruptcy court's equity jurisdiction." *Id.* Accordingly, there is no basis to treat a compulsory counterclaim differently from the way the Court treated the preference counterclaim in *Langenkamp*. By filing a proof of claim, the creditor foregoes the right to object to non-Article III adjudication of a compulsory counterclaim.

Recently, in a unanimous opinion, the Court addressed the profound importance of easily administrable jurisdictional schemes:

> [A]dministrative simplicity is a major virtue in a jurisdictional statute. . . . Complex jurisdictional tests complicate a case, eating up time and money as the parties litigate, not the merits of their claims, but which court is the right court to decide those claims. . . . Complex tests produce appeals and reversals, encourage gamesmanship, and, again, diminish the likelihood that results and settlements will reflect a claim's legal and factual merits. Judicial resources too are at stake.

Hertz Corp. v. Friend, – U.S. —, 130 S. Ct. 1181, 1193 (2010). The efficiency of a single adjudication of a creditor's claims and compulsory counterclaims thereto makes vastly greater sense than complicating and slowing down the bankruptcy process while further burdening already busy district courts and increasing costs to litigants.

CONCLUSION

Based upon the foregoing, the Court should reverse the judgment of the Ninth Circuit.

Respectfully submitted,

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Dated: November 15, 2010

AMICUS CURIAE BRIEF

No. 10-179

IN THE

Supreme Court of the United States

HOWARD K. STERN, EXECUTOR OF THE ESTATE OF VICKIE LYNN MARSHALL,

Petitioner,

v.

ELAINE T. MARSHALL, EXECUTRIX OF THE ESTATE OF E. PIERCE MARSHALL,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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INTEREST OF AMICI

Amici curiae are law professors with expertise in bankruptcy law, federal courts and federal jurisdiction. This case addresses important issues regarding the extent to which the judicial power of the United States can, consistent with the Constitution, be delegated to Article I bankruptcy courts. *Amici* have a professional interest in the proper application and development of the law in this area.[1]

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1. No counsel for a party authored this brief in whole or in part, and no such counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than the amici, or their counsel, made a monetary contribution intended to fund its preparation or submission. The parties have filed blanket waivers with the Court consenting to the submission of all amicus briefs.

STATEMENT

This case is not about bankruptcy jurisdiction. Bankruptcy jurisdiction is governed by 28 U.S.C. § 1334, and reaches as far as all matters "related to" a bankruptcy case. Bankruptcy *jurisdiction* is not at issue in this case.

Rather, this case is about limitations on the exercise of the judicial power of the United States by Article I judges. Congress has limited the extent of judicial power that can be exercised by Article I bankruptcy judges through the distinction between "core" matters that "arise under" the Bankruptcy Code[2] or "arise in" a bankruptcy case, on the one hand, and "non-core" matters that are "related to" a case, on the other.

The distinction is set out in 28 U.S.C. § 157. For "core" matters arising under the Code or arising in a bankruptcy case, bankruptcy courts are authorized to exercise the full range of judicial power of the United States and can enter final orders reviewable only by appeal. For "non-core" matters that are merely "related to" a bankruptcy case, bankruptcy courts cannot exercise the full extent of that power without the parties' express written consent, and may instead only enter proposed findings of fact and conclusions of law that are reviewable, *de novo*, by an Article III district court.[3] In either case, jurisdiction is present and the

2. 11 U.S.C. §§ 101 *et seq.* (hereinafter, the "Code").

3. *See* 28 U.S.C. §§ 157(c)(1) (de novo review), 158 (appellate review); G. Marcus Cole & Todd J. Zywicki, *Anna Nicole Smith Goes Shopping: The New Forum-Shopping Problem In Bankruptcy*, 2010 UTAH L. REV. 511, 531 (2010) (hereinafter, "*Forum-Shopping*") (discussing review).

matter can be heard by the bankruptcy court; the distinction is the type of order that can be entered by the bankruptcy court.[4] The question here is whether the counterclaim at issue can be considered a "core" matter "arising under" the Code or "arising in" a bankruptcy case for which a bankruptcy court can enter a final order.

Article III of the Constitution provides that "[t]he judicial Power of the United States, shall be vested in one supreme Court, and in such inferior Courts as Congress may from time to time ordain and establish," and that the judges of those courts must have life tenure (assuming "good Behavior") and receive undiminished compensation during that tenure. U.S. CONST. art. III, § 1. These protections ensure the independence of the judiciary, which is an "inseparable element of the constitutional system of checks and balances." *N. Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 58 (1982).[5]

4. Petitioner misapplies this concept. Pet. Br. at 35 ("splinter[s]" jurisdiction "into different forums"); 36 (requires district courts to determine counterclaims); 47 (citing *Alexander v. Hillman*, 296 U.S. 222 (1935), and implying the decision below requires Petitioner to "go to another court to recover [on the counterclaim]."). If jurisdiction is present under 28 U.S.C. § 1334 and referral made under 28 U.S.C. § 157(a), the matter can be heard by the bankruptcy court (unless removal or abstention is applied). The difference is in the type of order the bankruptcy court can enter.

5. *See* Rotunda & Nowak, 1 TREATISE ON CONSTITUTIONAL LAW: SUBSTANCE & PROCEDURE § 2.1 (4th ed. 2007) ("*Article I Courts*"; discussing the *Marathon* principle, *Thomas v. Union Carbide Agricultural Products, Inc.* and *Commodity Futures Trading Comm'n v. Schor*); *id.* § 3.7 ("*Sources of Federal Power—Bankruptcy*"; discussing *Marathon*).

Nevertheless, Congress may, pursuant to Article I, vest decision-making authority over certain disputes in tribunals that lack the attributes of Article III courts. *Thomas v. Union Carbide Agric. Prods., Inc.*, 473 U.S. 568, 583 (1986). Whether a congressional delegation of adjudicative functions to a non-Article III tribunal is constitutionally permissible "must be assessed by reference to the purposes underlying the requirements of Article III." *Commodity Futures Trading Comm'n v. Schor*, 478 U.S. 833, 847-48 (1986).

In 1978, Congress re-wrote the nation's bankruptcy laws, replacing the Bankruptcy Act of 1898 with the Code. Under the 1978 Code, bankruptcy courts had broad jurisdiction over "all civil proceedings arising under title 11 [the Code] or arising in or related to cases under title 11." 28 U.S.C. § 1471(b) (repealed 1984). The 1978 Code did not distinguish between "core" and "non-core" matters. Instead, bankruptcy courts had plenary jurisdiction over all proceedings "arising under" the Code or "arising in or related to" cases under the Code.

Marathon addressed whether that jurisdictional scheme violated Article III. After Northern Pipeline filed for bankruptcy, it brought suit in the bankruptcy court against Marathon on a state-law breach-of-contract claim. *Marathon*, 458 U.S. at 56. The state-law claim did not arise under the Code or arise in the bankruptcy case, but was "related to" the bankruptcy case because any recovery on the claim would have increased the estate's assets. *Id.* at 54, 71-72 (plurality). Under the 1978 Code, the bankruptcy court had plenary jurisdiction over proceedings "related to" the bankruptcy case. *Id.* at 54. The Court held that

permitting non-Article III bankruptcy courts to exercise plenary jurisdiction over state-law contract claims merely because those claims were "related to" the bankruptcy case contravened Article III because doing so removed "the essential attributes of the judicial power from the Article III district court and vested those attributes in a non-Article III adjunct." *Id.* at 87 (plurality opinion); *id.* at 91-92 (Rehnquist, J., concurring).

A plurality of four Justices concluded that there was a constitutionally significant difference between "public rights" matters "arising between the Government and persons subject to its authority" that historically could have been determined by Congress or the executive branch, on the one hand, and "private rights" matters, which include disputes between individuals arising under common law, on the other. *Id.* at 67-70. "Public rights" matters could under certain circumstances be constitutionally adjudicated by non-Article III tribunals. *Id.* at 69. But "private rights" matters generally could not. *Id.* at 70-71, 83-87.

In response to the constitutional concern articulated in *Marathon*, in 1984 Congress amended title 28 to limit the power of bankruptcy courts to enter final judgment to the type of "public rights" matters that *Marathon* suggested may be constitutionally adjudicated in an Article I court. The statute achieves this goal by distinguishing between "core" bankruptcy proceedings that "aris[e] under" the Code or "aris[e] in a case under" the Code, and "non-core" bankruptcy proceedings that are "otherwise related to" a case under the bankruptcy laws. 28 U.S.C. § 157. Today, any interpretation of 28

U.S.C. § 157 must be consistent with *Marathon*. This is especially so considering that Congress amended the Code in an effort to comply with *Marathon*.

The amended statute gives federal district courts original and exclusive jurisdiction over "all cases under title 11." 28 U.S.C. § 1334(a).[6] The amended statute also gives district courts original jurisdiction over "all civil proceedings arising under" the Code, "or arising in or related to cases under" the Code. 28 U.S.C. § 1334(b). District courts may refer any of those proceedings to a bankruptcy court. *Id.* § 157(a).[7] Bankruptcy courts have authority to enter final judgments only in "core" bankruptcy proceedings that "aris[e] under" the Code, or "aris[e] in a case under" the Code. *Id.* § 157(b)(1).[8] In contrast, for "non-core" matters that are only "related

6. There is no insolvency requirement for relief under present-day title 11, although such a requirement existed at times under prior bankruptcy laws. *See* Thomas E. Plank, *The Constitutional Limits Of Bankruptcy*, 63 TENN. L. REV. 487, 546 (Spring 1996) (historical analysis).

7. "All U.S. district courts, by operation of local rules, automatically refer bankruptcy petitions filed with their respective clerk of court's office to the district's bankruptcy court." *Forum-Shopping*, 2010 UTAH L. REV. at 530-31.

8. *Forum-Shopping*, 2010 UTAH L. REV. at 526 ("In order to have final order jurisdiction, the bankruptcy court must have before it a 'core' matter that also 'arises in' or 'arises under' a case under title 11. The distinction may appear to be a subtle one, but it is one of enormous consequence.") (footnote omitted); *id.* at 534 ("[T]he party asserting bankruptcy jurisdiction must demonstrate not only that the matter is 'core' within the meaning of § 157(b)(2), but also that it 'arises under' or 'arises in' a case under title 11.").

to" a bankruptcy case, bankruptcy courts cannot enter final judgments without the parties' express consent, and may only enter proposed findings of fact and conclusions of law subject to *de novo* review by the district court. *Id.* § 157(b)(1), (c).

Proceedings that "arise under" the Code involve rights created or determined by federal bankruptcy law. *See* 1 ALAN N. RESNICK & HENRY J. SOMMER, COLLIER ON BANKRUPTCY ¶ 3.01[3][c][i] (16th ed. 2010). Proceedings that "arise in a case" under the Code are matters that arise *only* in bankruptcy cases. *See id.* at ¶ 3.01[3][c][iv]. In short, proceedings that invoke substantive rights created by federal bankruptcy law or that could arise only in the context of a bankruptcy case are the kinds of "core" proceedings that a bankruptcy court may finally determine. 28 U.S.C. § 157(b)(1). Being creatures of federal creation unique to bankruptcy proceedings, these matters can be viewed as involving "public rights" that can be resolved by entry of final orders by Article I bankruptcy courts (when consistent with *Granfinanciera*, discussed *infra*).[9]

The Court's post-*Marathon* cases suggest that, if a state-law counterclaim to a proof of claim in bankruptcy can be considered a "core" proceeding that an Article I bankruptcy court may determine by entry of a final order, resolution of that counterclaim must be necessary to determine the allowance or disallowance of the underlying claim against the estate—*i.e.*, it is so

9. One view is that public rights matters require that the United States be a party to the litigation. For purposes of this case, *amici* discuss a broader rule.

intertwined with a function that the bankruptcy court must perform that it may properly be assigned to a non-Article III judicial officer. Those cases reveal that although a majority of the *Marathon* Court did not adopt the plurality's reasoning that the public/private right distinction was dispositive, the basic distinction drawn in *Marathon* between matters of public right that are at the core of the bankruptcy process, and matters of private right that are not, is still viable.

Thomas v. Union Carbide Agricultural Products, Inc., considered the constitutionality of provisions of the Federal Insecticide, Fungicide, and Rodenticide Act and whether disputes over related licensing fees could be decided by a non-Article III tribunal with limited Article III review. 473 U.S. 568 (1986). To evaluate the constitutional propriety of this statutory scheme, the Court adopted a balancing test, under which the public/private right determination was one important factor. *Id.* at 587. The Court concluded that although the license fee disputes were between private parties, the licensing provision had "many of the characteristics of a 'public right'" because it was an integral part of a federal regulatory scheme. In those circumstances, the Court concluded that "Congress may create a seemingly private right that is so closely integrated into a public regulatory scheme as to be a matter appropriate for agency resolution with limited involvement by the Article III judiciary." *Id.* at 593-94.

Commodity Futures Trading Commission v. Schor, considered the constitutionality of a scheme under which non-Article III tribunals could adjudicate state-law counterclaims between private parties. 478 U.S. 833

(1986). Under the Commodity Exchange Act, the Commodity Futures Trading Commission ("CFTC") administered a reparations procedure under which customers of commodity brokers could seek monetary redress for violations of the Act. As part of adjudicating reparations claims, the CFTC was also permitted to adjudicate state-law counterclaims by brokers arising out of the same transaction or occurrence. *Id.* at 837. Applying the *Thomas* balancing test, the Court found that this scheme did not violate Article III, even though the state-law counterclaim was a matter of "private right" "at the 'core' of matters normally reserved to Article III courts." *Id.* at 853. The Court concluded that the scheme was permissible because the CFTC's jurisdiction was limited to "a narrow class" of state-law counterclaims arising out of the same transaction or occurrence, resolution of which was "a necessary incident to the adjudication of federal claims." *Id.* at 865, 856-57.[10]

Granfinanciera, S.A. v. Nordberg, addressed whether a person who had not submitted a claim against a bankruptcy estate had a right to a jury trial when sued by a bankruptcy trustee to recover alleged fraudulent transfers from the debtor. 492 U.S. 33, 36 (1989). The Court held that the defendant was entitled to a jury trial, relying on the public/private right distinction. Notably, Congress had designated fraudulent transfer actions as "core proceedings" in 28 U.S.C. § 157(b)(2)(H), strongly suggesting that Congress viewed them as

10. Another consideration was that the CFTC's decisions were reviewable *de novo* in federal court. *Id.* at 852-56. *De novo* review was applied by the district court in this case.

"public rights" matters under *Marathon*. Nonetheless, the Court concluded that a fraudulent transfer action was not a matter of "public right" and instead, was a matter of "private right" because historically it was a common-law action that more closely resembled a contract suit brought by a debtor to augment the estate than creditors' claims to distributions from the estate. *See id.* at 55-56.

Accordingly, the Court held that, where the defendant had not filed a claim against the estate, it was entitled to a jury trial in a fraudulent transfer action. *See id.* at 64. By contrast, where a creditor has filed a proof of claim, and a trustee brings a preference action against the creditor such that resolution of those claims is intertwined and "integral" to the public right involved in the claims allowance and disallowance process, a jury trial is not required. *Langenkamp v. Culp*, 498 U.S. 42, 44 (1990); *see also Katchen v. Landy*, 382 U.S. 323, 330-31 (1966) (claim could be neither allowed nor disallowed until preference was determined; therefore, whether creditor has received voidable preference is "part and parcel of the allowance process" subject to summary adjudication by bankruptcy court).

The Court's approach since *Marathon* retains the public/private right distinction and permits a non-Article III tribunal to adjudicate state-law "private rights" only where the state-law claim is so intertwined with a public right that resolution of the state-law claim is necessary to determine federal rights. Likewise, here, *amici* submit that a state-law counterclaim can be a "core" proceeding "arising in a case under" the Code, that a bankruptcy judge may finally determine under

28 U.S.C. § 157(b)(2)(C), only if the counterclaim is so closely related to the proof of claim that resolution of the counterclaim is necessary to resolve the allowance or disallowance of the underlying claim.

Finally, in drawing the line of demarcation between what can and cannot be permissibly considered a "core" counterclaim "arising in" a bankruptcy case within the scope of 28 U.S.C. § 157(b)(2)(C), *amici* submit that two practical points should be kept in mind.

First, Petitioner emphasizes that this case involves a "compulsory" counterclaim and asks that the Court infer from the "compulsory" label that the counterclaim is necessarily a core matter because it "had to" be asserted. *Amici* submit that the compulsory label is not in and of itself relevant. Moreover, Petitioner contends that "compulsory counterclaims arise out of the same *transaction* that the creditor, by filing the proof of claim, submitted to the bankruptcy court for resolution and constitute potential affirmative defenses to the creditor's claim." Pet. Br. at 45 (emphasis supplied). This is an inaccurate and restrictive description of what constitutes compulsory counterclaims in federal court litigation, and as a result understates the rule Petitioner advocates.

Rule 13(a) of the Federal Rules of Civil Procedure, which governs compulsory counterclaims, embodies a rule of convenience. FED. R. CIV. P. 13. It has been broadly construed. Its goals are judicial efficiency and a desire to avoid a multiplicity of suits. It is a *jurisdictional* concept in that it brings into federal court certain state-law counterclaims. 6 WRIGHT-MILLER-KANE,

FEDERAL PRACTICE AND PROCEDURE § 1409 at 49-50 (West 2010) (noting jurisdictional distinctions between compulsory and permissive counterclaims). The most frequently used test for whether a counterclaim is "compulsory" considers whether the counterclaim is "logically related" to the underlying claim, or arises out of "the same transaction or occurrence[,]" or a series of transactions or series of occurrences. *Id.* at § 1410 (generally).[11]

Amici submit that the policy-driven analysis of whether the "compulsory" label applies in a given case has little if any relevance to the question of whether a counterclaim should be considered "core." Those considerations may be relevant in the context of an Article III court's exercise of its plenary adjudicative authority, but are not relevant in the context of a non-Article III bankruptcy court's function of administering the Code. Where the power of a bankruptcy court to enter a final order is at issue, *amici* submit that the rule of convenience contained in Rule 13(a) is not a relevant consideration.[12]

11. *See Moore v. N.Y. Cotton Exch.*, 270 U.S. 593, 609-10 (1926) ("'Transaction' is a word of flexible meaning. It may comprehend a series of many occurrences, depending not so much on the immediateness of their connection as upon their logical relationship . . ."); *Maln*owski v. N.Y. State Dep't of Labor*, 156 F.3d 131, 133 (2d Cir. 1998) ("a transaction 'may comprehend a series of many occurrences, depending not so much upon the immediateness of their connection as upon their logical relationship.'").

12. *See Forum-Shopping*, 2010 UTAH L. REV. at 532 ("Although bankruptcy jurisdiction is necessarily broad, it does not follow that the powers of the bankruptcy court are likewise broad.") (discussing *Wood v. Wood (In re Wood)*, 825 F.2d 90 (5th Cir. 1987)).

Second, *amici* believe it is important to bear in mind the process by which claims can be pursued by creditors in bankruptcy cases, because it is only through the pursuit of an underlying claim that this case differs from *Marathon*.

It is very easy to file claims in bankruptcy cases. As a creditor, you typically get a claim form in the mail. If you are not mailed a form, they are available for free on-line.[13] Neither the form nor its instruction sheet say anything about counterclaims or jurisdiction. You fill out the one-page form, attach to it copies of your invoices or other evidence of the debt, and then mail it back. In many cases, you can electronically file claims, and need not even incur the expense of a stamp. It is that simple.

The broad scope of the compulsory counterclaim rule and the ease with which claims can be asserted, considered together, reveal that construing 28 U.S.C. § 157(b)(2)(C) as permissibly reaching all compulsory counterclaims would constitute an extremely broad delegation of the full range of judicial power of the United States to a non-Article III court. The following hypothetical fact pattern makes the point:

- You sell widgets.

- Over the years, you have sold two types of widgets: old widget A, and new widget B.

13. *See* UNITED STATES COURTS, BANKRUPTCY FORMS, http://www.uscourts.gov/FormsAndFees/Forms/BankruptcyForms.aspx (last visited December 15, 2010).

- You have a contract with a large corporation to sell to it any kind of widgets you make.

- After years of buying widget A, your customer stopped ordering that kind of widget two years ago. Since then, it has only ordered widget B.

- You sent a shipment for $50 worth of widget B to the corporation. You were not paid. Thereafter, the corporation files bankruptcy, even though it is not insolvent.

- A one-page claim form is mailed to you. You fill it out, put a stamp on it, and mail it back.

- You have submitted to bankruptcy court jurisdiction to have your claim determined. Resolution of your claim is a "core" matter.

Simple enough. But what happens next identifies the problem with Petitioner's reading of the statute:

- Responding to your $50 claim for widget B sales, debtor counterclaims for $100 million.

- The counterclaim alleges that widget A the debtor bought years ago – not the widgets on which your claim is based – was defective and caused the debtor to suffer tremendous losses. You had no idea this counterclaim, or the facts underlying it, existed.

- The counterclaim can be heard by the bankruptcy court because jurisdiction is present under 28 U.S.C. § 1334 and referral is made under 28 U.S.C. § 157(a).

- The debtor contends that because both matters arise out of the same contract, the counterclaim is compulsory and, thus, a "core" matter under 28 U.S.C. § 157(b)(2)(C). The bankruptcy court agrees, and you have lost your right to have an Article III court adjudicate the counterclaim.

The distinction between the extent of judicial power that has been granted to Article III courts, and that which can be delegated to Article I courts, is not so insignificant.

SUMMARY OF ARGUMENT

With *Marathon* as a backdrop, the basic question presented by this case is whether and where a line should be drawn between: (i) counterclaims that are "core" matters "arising under" or "arising in" that can be decided by entry of a final judgment by a bankruptcy court; and (ii) counterclaims whose relationship with the underlying bankruptcy claim is too tenuous to fit within the concept of "core" bankruptcy matters "arising in" a bankruptcy case and that are, instead, merely "related to" a bankruptcy case. In either case, jurisdiction is present but the extent of judicial power that can be exercised by Article I bankruptcy courts differs.

Amici submit that 28 U.S.C. § 157(b)(2)(C) should be construed to provide that when a counterclaim *must* be resolved in order for the underlying claim against the estate to be determined, the counterclaim can be a "core" matter for which bankruptcy courts can enter final orders reviewable only by appeal. Counterclaims that *do not* have to be resolved in order for the

underlying claim to be resolved are not core matters "arising under" title 11 or "arising in" a bankruptcy case. For such counterclaims, bankruptcy courts may exercise "related to" jurisdiction only, and may enter proposed findings of fact and conclusions of law that are reviewable *de novo* by an Article III district court.

This reading of the statute is consistent with a close reading of the Court's Article I jurisprudence. Moreover, this reading of the statute is based upon an analysis of the distinction between Article I and Article III that is grounded in context. *Amici* respectfully submit that when this analytical framework is applied, Petitioner's counterclaim should be considered a non-core matter and that the decision of the court of appeals should be affirmed.

ARGUMENT

I. Article I Courts May Finally Determine State-Law Counterclaims When Necessary To Resolve The Claim To Which It Responds

A. Context: Bankruptcy As Compared With Limited Legislative Schemes

There are three areas where the use of Article I tribunals has been permitted: (i) territorial courts; (ii) courts-martial; and (iii) legislative courts and administrative agencies created by Congress to adjudicate matters involving "public rights." *Marathon*, 458 U.S. at 65-66. Bankruptcy matters fall within the third category.

The difficulty in discerning the boundaries between what constitute "public rights" and "private rights" in the context of the Code arises out of the unique nature of the bankruptcy laws, the state-law nature of most claims, and the broad reach of bankruptcy jurisdiction.

Generally, Article I is used to establish judicial or quasi-judicial tribunals within the sphere of legislative courts and federal administrative and regulatory agencies. Bankruptcy is unique when viewed against this backdrop because the reach of bankruptcy jurisdiction greatly exceeds that which is generally granted to administrative agencies, and the scope of matters and claims that fall within bankruptcy jurisdiction is likely more expansive than that which is delegated to any administrative agency setting. *See* 28 U.S.C. § 1334. Thus, although precedent addressing the delegation of judicial power to administrative agencies is a useful reference, *amici* submit that heightened sensitivity is required in the bankruptcy context because of the exceptionally broad grant of jurisdiction.

Through the Code and Rules, Congress has put in place a framework for the processing of claims against a bankruptcy estate. This is consistent with the fundamental *in rem* nature of bankruptcy proceedings. *Cent. Va. Comm. Coll. v. Katz*, 546 U.S. 356, 362 (2006) ("Bankruptcy jurisdiction, at its core, is *in rem*."). The breadth of the "claims" from which a debtor is given relief through a discharge is exceptionally broad. *See* 11 U.S.C. §§ 101(5), 1141(d)(1), 1228(a), 1328(a). Most commonly, creditors seeking a distribution from the *res* in possession of the bankruptcy court assert state-law claims. *See Travelers Cas. & Sur. Co. of Am. v. Pac. Gas*

& Elec. Co., 549 U.S. 443, 451 (2007); *Butner v. United States*, 440 U.S. 48, 57 (1979).

This unique statutory framework makes elusive a precise definition of what are properly considered "public rights" in the bankruptcy context. Decisions from the Court have not fully resolved this line-drawing exercise. In *Marathon*, the Court described two types of bankruptcy matters the Court viewed as being squarely on opposite sides of the line: (i) matters involving "the restructuring of debtor-creditor relations"[14] and (ii) "the adjudication of state-created private rights[.]" *Marathon*, 458 U.S. at 71. Thus, in *Marathon*, since the non-debtor party had not asserted a claim against the bankruptcy estate, the Court held that a state-law claim by the debtor against its contract counter-party could not be fully adjudicated by the non-

14. Subsequent decisions retreated from the suggestion that an open-ended, broad category of matters–"restructuring of debtor-creditor relations"–qualifies. *Granfinanciera*, 492 U.S. at 56 n.11. Petitioner relies on this categorical description. Pet. Br. at 56-57 ("Accordingly, claims allowance *and* the adjustment of the debtor-creditor relationship is a scheme of congressionally-created rights involving a specialized area where Congress has plenary Article I power.") (emphasis supplied). In doing so, Petitioner effectively seeks review of 28 U.S.C. § 157(b)(2)(O), which addresses "the adjustment of the debtor-creditor . . . relationship[.]" Review was not sought, nor was *certiorari* granted, with respect to 28 U.S.C. § 157(b)(2)(O).

Tethering the "public right" distinction to the federal statute for claims allowance – 11 U.S.C. § 502 – rather than to a broad, ill-defined categorical description, is the better approach. Even so, 11 U.S.C. § 502 does not provide a federal right to pursue *counterclaims*; rather, it provides a mechanism for pursuing *claims* against the *res*.

Article III bankruptcy court. It was a "private right" action to augment the *res*, not a claim against the *res*.

Here, Respondent filed a claim against the bankruptcy estate. The assertion of this claim implicated the claims allowance and disallowance process; but even so, characterizing a claim against a bankruptcy estate as a "public right" is an awkward fit. The defamation claim against the *res* here arises under state law. Congress did not create this right, nor is the Government a party to it. Thus, the "claim," in and of itself, falls outside any commonly accepted description of a "public right." However, Congress created the statutory framework through which claims against the *res* are processed. With context in mind, the allowance or disallowance pursuant to 11 U.S.C. § 502 of a state-law defamation claim against the bankruptcy estate can be viewed as implicating a "public right" because absent the framework put in place by Congress, the right to share in the bankruptcy estate through an allowed claim would not exist.

Other rights and claims, created by the Code, fall within the "public rights" domain as well. Claims that a debt is nondischargeable, claims of exemptions, and assertion of an entitlement to a discharge, are matters that can be considered "public rights." *See* 11 U.S.C. §§ 522, 523, 1141, 1228, 1328. These matters "arise under" the Code or "arise in" a bankruptcy case. The claim asserted by Petitioner is none of those things. Rather, it is a state law tort claim for damages personal to Petitioner that may augment the estate, much like the claim that was asserted in *Marathon*. There is no provision in the Code for the "recovery of estate

counterclaims" or "recovery on causes of action in favor of the estate." Rather, where state-law counterclaims are involved, the federal statutory right implicated is a *creditor's* right to have its claim against the bankruptcy estate allowed or disallowed under 11 U.S.C. § 502. Since 11 U.S.C. § 502 is the federal statutory provision implicated, the question here is whether Petitioner's private right of action counterclaim can nonetheless be adjudicated to judgment by the Article I bankruptcy court not on its face, but rather, as incident to the allowance or disallowance of the proof of claim filed by Respondent.

Interpreting 28 U.S.C. § 157(b)(2)(C) consistently with *Marathon* reveals that the statute cannot be construed to provide that *all* "counterclaims by the estate against persons filing claims against the estate" are core proceedings. Such an interpretation of the statute, divorced from the "arising in" limitation Congress created in response to *Marathon*, would necessarily encompass not only counterclaims that involve rights under federal bankruptcy law ("arising under") and that arise *only* in the context of a bankruptcy case ("arising in"), but also counterclaims that are only "related to" cases under the Code. It would include private rights matters having nothing to do with (i) claims against the *res* in possession of the bankruptcy court or (ii) the allowance or disallowance of claims that is the focus of the Code and Rules.[15] Reading the statute

15. Such a rule has "no limiting principle." *Marathon*, 458 U.S. at 73-74; *see* Jeffrey T. Ferriel, *Constitutionality Of The Bankruptcy Amendments And Federal Judgeship Act Of 1984*, 63 AM. BANKR. L.J. 109, 135-36 (Spring 1989) (hereinafter, "*Constitutionality Of The Bankruptcy Amendments*") (discussing transactional approach, noting that transactional counterclaims can be litigated in a claim objection).

to mean that all counterclaims are "core" matters based on "public rights" (even where they are, substantively, private rights matters) would directly contravene *Marathon* and the Article III concerns that the amended statutory scheme was intended to address.[16] It would ignore *context*, the basic and fundamental nature of bankruptcy proceedings as being a process for resolving claims against a *res*, and the Article I implications of the broad jurisdictional grant in 28 U.S.C. § 1334.

B. Not All Counterclaims Can Be "Core"

In order to avoid the constitutionally dubious conclusion that all counterclaims can be "core" proceedings that a bankruptcy court may finally determine, *amici* submit that the statute should be construed to provide that a counterclaim can be a "core" proceeding if resolution of that counterclaim is necessary as part of the allowance or disallowance of the underlying claim against the estate. *See Crowell v. Benson*, 285 U.S. 22, 62 (1932) ("[When] a serious doubt of constitutionality is raised [about an act of Congress], it is a cardinal principle that this Court will first ascertain whether a construction of the statute is fairly possible by which the question may be avoided.").

A tortious interference counterclaim does not "arise under" the Code because it is a matter of state law and no provision in title 11 provides for the allowance or disallowance of *counter*claims. However, title 11 does

16. It would also be contrary to *Granfinanciera*, discussed *infra* at Point I.B.

provide for the allowance and disallowance of claims against the bankruptcy estate by creditors, and the allowance of claims against the *res* can fairly be described as a "public right." 11 U.S.C. § 502. Thus, under the requirement for "arising in a case" under the Code, a state-law counterclaim might be viewed as a public right "arising in" a bankruptcy case if it is a necessary incident to the claim allowance process. But the extent of possible counterclaims is a matter of *in personam* rights that extends well beyond matters responsive to, or dispositive of, claims against the *res*. This raises the question of whether filing a claim against the *res* categorically transforms all counterclaims from private rights matters into public rights matters.

In resolving the question of whether private rights matters can be categorically recharacterized as public rights/core matters, *Granfinanciera v. Nordberg*, 492 U.S. 33 (1989), is instructive. In *Granfinanciera*, the Court addressed fraudulent transfer claims brought by a bankruptcy estate against parties that had not filed claims against it, and whether those claims were "core" matters that could be determined by a bankruptcy court without trial by jury.

In analyzing whether a Seventh Amendment right to a jury trial existed, the Court analyzed whether the fraudulent transfer action was a matter of "public rights" that could be assigned to a non-Article III court. The reason for this analysis was straightforward:

> [I]f a statutory cause of action, such as respondent's right to recover a fraudulent conveyance under 11 U.S.C. § 548(a)(2), is not

> a "public right" for Article III purposes, then Congress may not assign its adjudication to a specialized non-Article III court lacking "the essential attributes of the judicial power."

Granfinanciera, 492 U.S. at 53.

Addressing the public/private right distinction, the Court found that the cause of action in 11 U.S.C. § 548(a)(2) was a private, rather than public, right. Notwithstanding that the cause of action was a matter of statute under the Code, the Court based its finding on historical analysis of fraudulent transfer actions. *Id.* at 55-56. The Court stated:

> There can be little doubt that fraudulent conveyance actions by bankruptcy trustees–suits which, we said in *Schoenthal v. Irving Trust Co.*, 287 U.S. at 94-95, 53 S.Ct. at 51 (citation omitted), "constitute no part of the proceeding in bankruptcy but concern controversies arising out of it"–are quintessentially suits at common law that more nearly resemble state-law contract claims brought by a bankruptcy corporation to augment the bankruptcy estate than they do *creditors' hierarchically ordered claims to a pro rata share of the bankruptcy res. See Gibson* 1022-1025. They therefore appear matters of private rather than public right.

Id. at 56 (emphasis supplied); *see Marathon*, 458 U.S. at 72 n.26 ("This claim may be adjudicated in federal court on the basis of its relationship to the petition for

reorganization. But this relationship does not transform the state-created right into a matter between the Government and the petitioner for reorganization. Even in the absence of the federal scheme, the plaintiff would be able to proceed against the defendant on the state-law contractual claims.") (internal citations omitted). Thus, the cause of action could not be adjudicated to final judgment by an Article I bankruptcy court without respecting the defendant's right to a jury trial, because the action was a matter of "private rights."[17] The "core" label didn't matter; the substance of the claim did.

The same reasoning applies here. Although Congress has included counterclaims by the estate in a list of "core" matters, the fact remains that state-law counterclaims that will augment the estate, but that need not be resolved as part of a claim against the estate, are matters of private right, as *Granfinanciera* confirms. Matters of private right that are not intertwined with matters of public right (*e.g.*, the allowance of claims) such that resolution of the public right requires resolution of the private right, cannot be determined by entry of a final judgment by an Article I court. That is precisely the case here.

C. *Schor* and *Katchen*

Petitioner relies on *Commodity Futures Trading Commission v. Schor*, 478 U.S. 833 (1986), to support his position, but context is important. In *Schor*, the

17. The Court did not address whether permitting a jury trial to be held by an Article I court would satisfy the requirements of Article III. *Granfinanciera*, 492 U.S. at 50.

underlying claim was created by federal law. Schor asserted a reparations complaint against his broker arising out of his broker's alleged violations of the Commodity Exchange Act ("CEA") in handling Schor's accounts. Being a federally-created right, Congress provided that the reparations claim was to be heard by the Commodity Futures Trading Commission ("CFTC"), an Article I tribunal.

Schor's broker counterclaimed. The substance of the counterclaim is important to understanding the holding in *Schor*. It was a state law claim. After Schor's account was liquidated there was a debit balance, and the broker sought payment of that balance through the counterclaim. The claim and counterclaim arose out of the same account. The counterclaim alleged that the debit balance was a valid debt owed by Schor. Schor disagreed, and argued that the debit balance "was the result of [the broker's] numerous violations of the CEA." *Schor*, 478 U.S. at 837. Essentially, Schor said he *should not* have to pay the debit charges, and the broker said that Schor *should* have to pay the charges. The claims were based on the same debt. The success of one dictated the failure of the other.[18]

The Court upheld the authority of the CFTA to adjudicate state-law counterclaims "aris[ing] out of the

18. *See Constitutionality Of The Bankruptcy Amendments*, 63 Am. Bankr. L.J. at 136 (the counterclaim was "the only likely counterclaim that will be brought in a reparations proceeding [and that] the broker's right to recover the balance . . . is likely to turn more on resolution of the facts alleged by the customer in the reparations proceeding than on any independent factual basis").

transaction or occurrence or series of transactions or occurrences set forth in the complaint." *Schor*, 478 U.S. at 837 (quotations omitted). From this, Petitioner argues that the bankruptcy court below could enter a final order on Petitioner's counterclaim, because it was a compulsory counterclaim, and the test for whether a counterclaim qualifies for the "compulsory" label is the equivalent of the language used in the statute at issue in *Schor*.

Petitioner's argument ignores context. The reparations claim asserted in *Schor* was in a narrow class of statutory claims created by federal law. That is not the case here, and it is unrealistic to suggest that it would be the case in any bankruptcy proceeding, because the overwhelming majority of claims in bankruptcy are based on state law. Moreover, resolution of the counterclaim in *Schor* was part and parcel of resolution of the underlying claim. Resolution of one necessarily resolved the other. That is not the case here. Here, the claim was determined on November 5, 1999, when Petitioner was granted summary judgment, but the bankruptcy court did not rule on the counterclaim until September 27, 2000, nearly one year later. PA18-19. Here, one had nothing to do with the other. The rule from *Schor*, viewed alongside its facts, is not nearly as broad as Petitioner suggests by arguing that it controls here.

Nor should *Schor* be read so expansively. The dissent, authored by Justice Brennan (who authored the plurality opinion in *Marathon*), noted that although *Schor* involved a narrow set of facts, the rule from *Schor* could be broadened. *Schor*, 478 U.S. at 865-66. Justice Brennan warned that an expansive reading of *Schor*

would put the protections of Article III on a slippery slope that could lead to their erosion and dilution. *Id.* at 866. That erosion is precisely what Petitioner seeks here.[19] Bearing in mind that Justice Brennan authored the plurality opinion in *Marathon* that addressed the public/private right question in the bankruptcy context, his concerns in *Schor* reinforce the conclusion that 28 U.S.C. § 157(b)(2)(C) should not be read as expansively as its text (all counterclaims), or even as expansively as Petitioner suggests (at a minimum, all compulsory counterclaims).

Katchen v. Landy, 382 U.S. 323 (1966), is consistent with *Schor*. In *Katchen*, a creditor filed a claim and in response the trustee asserted a preferential transfer action. The Bankruptcy Act in effect at the time provided that before a creditor could be given an allowed claim, it had to pay back to the estate the amount of any preferential payment it received. The question before the Court was whether the Bankruptcy Act enabled the preference action, and an order requiring repayment to the estate, to be summarily decided as part of the allowance or disallowance of the claim that was filed against the *res*, without a plenary action. The Court held that it *could* be summarily tried, because the objection had to be fully resolved before the claim could be allowed. It was part and parcel of the claims allowance process. *Id.* at 336. Indeed, the statute implicated in *Katchen* was entitled "Proof and Allowance of Claims."

19. Query whether jurisdiction would exist if the broker alleged that Schor defamed him years ago when, after Schor incurred losses, he told friends the broker gave bad advice, and as counterclaims the broker sought recovery for defamation and tortious interference with prospective economic advantage.

See id. at 330-31 (discussing 11 U.S.C. § 93(g) (1964 ed.)).[20]

In *Katchen*, the Court observed:

> [The] power to allow or to disallow claims includes full power to inquire into the validity of any alleged debt or obligation of the bankrupt upon which a demand or a claim against the estate is based. This is essential to the performance of the duties imposed upon it. . . . The whole process of proof, allowance, and distribution is, shortly speaking, an adjudication of interests claimed in a *res*, and thus falls within the principle quoted above that bankruptcy courts have summary jurisdiction to adjudicate controversies relating to property within their possession.

Id. at 330 (internal quotations and citations omitted). This passage emphasizes that the bedrock bankruptcy function of resolving claims focuses on the *res*, not claims to augment the estate such as the claims at issue here.

The Court also noted that lower court decisions "[upholding] summary jurisdiction to grant affirmative relief on related counterclaims *that would also be defenses to the claim*" were consistent with its holding

20. Subsection (g) provided: "The claims of creditors who have received or acquired preferences . . . void or voidable under this Act, shall not be allowed unless such creditors shall surrender such preferences . . . ."). *See* App. A, LAWRENCE P. KING, COLLIER ON BANKRUPTCY, App. Pt. 3(a), at 3-47 and 3-48 (15th ed. revised 2010).

in *Katchen*. *Id.* at 336 n.12 (emphasis supplied). The Court's later holding in *Schor* is consistent with this aspect of *Katchen*, because in *Schor*, resolution of the claim necessarily determined the counterclaim, and vice versa. *Schor*, 478 U.S. at 856 ("The CFTC adjudication of common law counterclaims is incidental to, and completely dependent upon, adjudication of reparations claims created by federal law, and in actual fact is limited to claims arising out of the same transaction or occurrence as the reparations claim.").

Amici submit that *Schor* and *Katchen* provide that when resolution of a counterclaim is necessary for a bankruptcy court to fulfill its obligations under 11 U.S.C. § 502 to determine the allowance or disallowance of claims against the estate, or resolution of the claim resolves the counterclaim, it can be a core matter consistent with the Court's "public rights" jurisprudence. Conversely, if the proof of claim and counterclaim are *not* so intertwined that the counterclaim implicates the claim allowance statute, the counterclaim cannot be transformed into a public rights "core" matter. Rather, it is then a non-core matter that implicates "related to" jurisdiction alone.[21]

21. The Code must be construed to respect state law rights except for rare circumstances in which bankruptcy requires otherwise. *Butner v. United States*, 440 U.S. 48, 55 (1979) ("Unless some federal interest requires a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding. Uniform treatment of property interests by both state and federal courts within a State serves to reduce uncertainty, to discourage forum shopping, and to prevent a party from receiving a windfall merely by reason of the happenstance of bankruptcy.") (citation omitted).

Rather than tethering the public/private right distinction to the federal statute, Petitioner relies on a broad, categorical description of what can constitute core matters. Petitioner argues: "[C]laims allowance *and* the *adjustment of the debtor-creditor relationship* is a *scheme* of congressionally-created rights involving a specialized area where Congress has plenary Article I power." *See* Pet. Br. at 56-57 (emphasis added). The Court previously declined the invitation presented by Petitioner's argument–to find that a category of matters, as open-ended and broad as "the restructuring of debtor-creditor relations," should be considered public rights. *See Granfinanciera*, 492 U.S. at 56 n.11. *Amici* submit that grounding the "public right" distinction in the federal *statute* – 11 U.S.C. § 502 – is the more appropriate and supportable approach.[22]

22. There is confusion in Petitioner's approach. At times, Petitioner advocates a narrow rule. *See* Pet. Br. at 16 ("integrally-related counterclaims"). At other times, Petitioner advocates an expansive rule. *See* Pet. Br. at 32 ("core bankruptcy function of restructuring *and* adjusting debtor-creditor rights") (emphasis supplied); 56 ("claims allowance *and* the adjustment of the debtor-creditor relationship . . .") (emphasis supplied). 28 U.S.C. § 157(b)(2)(O) addresses "the adjustment of the debtor-creditor . . . relationship" and is not implicated by the questions for which the Court granted *certiorari*. *See* n.11, *supra*. Regardless, courts have read *Marathon* as limiting 28 U.S.C. § 157(b)(2)(O). *See Wood v. Wood (In re Wood)*, 825 F.2d 90, 95-98 (5th Cir. 1987); *Forum-Shopping*, 2010 UTAH L. REV. at 526 ("[I]t is conceivable that a bankruptcy court, in making the determination as to whether a matter is a 'core' proceeding, might rely on this language and sweep into its final order jurisdiction a case wholly reliant upon state law and rights created by it, thereby elevating its powers to those of an Article III federal court.").

II. *Marathon's* Concerns About An Independent Judiciary Are Not Eliminated By The Present-Day Bankruptcy Code

Petitioner suggests that because the present-day statutory framework provides that bankruptcy judges are appointed and removed by Article III judges, that the independence of the judiciary concerns highlighted in *Marathon* are *de minimis*. Pet. Br. at 55-59. This is incorrect.

As the Court recognized in *Marathon*:

> Periodic appointments, however regulated, or by whomsoever made, would, in some way or another, be fatal to [the courts'] necessary independence. If the power of making them was committed either to the Executive or legislature, there would be danger of an improper complaisance to the branch which possessed it; if to both, there would be an unwillingness to hazard the displeasure of either; if to the people, or to persons chosen by them for the special purpose, there would be too great a disposition to consult popularity, to justify a reliance that nothing would be consulted but the Constitution and the laws.

Marathon, 458 U.S. at 58-59 (internal quotations omitted) (quoting THE FEDERALIST No. 78, at 489 (Alexander Hamilton) (H. Lodge ed., 1888)); *see Schor*, 478 U.S. at 859-60 (Brennan, J., dissenting).

More directly addressing Petitioner's contention, the Court noted:

> The guaranty of life tenure insulates the individual judge from improper influences not only by other branches but by colleagues as well, and thus promotes judicial individualism.

Marathon, 458 U.S. at 59 n.10; *see also Schor*, 478 U.S. at 860-61 (Brennan, J., dissenting) (noting Alexander Hamilton's observation "[t]hat inflexible and uniform adherence to the rights of the Constitution, and of individuals, which we perceive to be indispensable in the Courts of justice can certainly not be expected from Judges who hold their offices by a temporary commission.") (*quoting* THE FEDERALIST No. 78, at 546 (Alexander Hamilton) (H. Dawson ed. 1876)) (internal quotations omitted); *Forum-Shopping*, 2010 UTAH L. REV. at 538-39 (noting problems with reappointment system).

The structural protections of the Constitution requiring that the adjudication of private rights matters be reserved for the Article III judiciary remain important in the bankruptcy context regardless of the fact that, today, bankruptcy judges are appointed by their colleagues instead of by the Executive or legislature. This very circumstance was foretold by Justice Brennan in *Marathon*, and further "incremental erosion" of these structural protections was warned against by Justice Brennan in *Schor*.

Faced with a choice, Congress chose not to create a system within which bankruptcy judges would be given

Article III status. Instead, Congress chose to create a system in which there are limitations. Those limitations cannot be ignored.

III. Petitioner's Counterclaim Was Not Integral To Allowance Or Disallowance Of Claims Against The Estate

Amici submit that Petitioner's tortious interference claim can only be a "core" proceeding "arising in" a case under the Code if resolution of the counterclaim was necessary in order to resolve the allowance or disallowance of Respondent's claim against the estate.

Here, the Court of Appeals found it to be an "inescapable conclusion" that "resolution of [Petitioner's] counterclaim was not a necessary predicate to the bankruptcy court's decision to allow or disallow [Respondent's] claim." PA52. Petitioner disagrees, contending that success on the tortious interference counterclaim would have "establish[ed] the affirmative defense of truth" to Respondent's defamation claim. Pet. Br. at 14.

In dissecting Petitioner's argument, it is important to recognize that the *defense* is separate and distinct from the *counterclaim*. ER-938, 941-54.[23] Petitioner

23. The counterclaims were varied, based upon different theories and sought varied relief. *See Marshall v Marshall*, 275 B.R. 5, 9 (C.D. Cal. 2002) (counterclaims for fraudulent transfer, injunction, conversion, tortious interference, breach of fiduciary duty, abuse of process, fraud, promissory estoppel, breach of contract (third-party beneficiary), imposition of constructive trust, accounting, indemnity and contribution).

blurs this distinction, combining the two separate concepts into one: "success on [Petitioner's] counterclaim would necessarily defeat [Respondent's] proof of claim by establishing the affirmative defense of truth[.]" Pet. Br. at 14. This is a flaw in Petitioner's argument, not a strength. In substance, Petitioner argues that resolution of the tortious interference counterclaim would have "brought with it" resolution of the affirmative defense.[24] Clever wordsmithing, but this bootstraps the *counterclaim* (that both the district court and court of appeals said had an attenuated relationship to the underlying claim) to the affirmative *defense* (that has a direct relationship to it). The stand-alone *defense* was all that might have been necessary to resolve as part of the allowance or disallowance of the claim. The counterclaim was not. Indeed, the history of this case makes this clear: the bankruptcy court granted Petitioner summary judgment on Respondent's claim on November 5, 1999, and it was nearly a year later (September 20, 2000) before it ruled on the counterclaim. PA18-19.

Amici submit that for the reasons noted above, and regardless of the fact that Petitioner's counterclaim was found to satisfy the rules of convenience and judicial economy on which the compulsory counterclaim rule is based, resolution of Petitioner's counterclaim was not necessary to resolve the allowance or disallowance of Respondent's claim against the estate. PA18-19 (noting

24. Whether this is correct is debatable when the one-sentence affirmative defense, *see* ER-938, is compared with the nineteen paragraphs detailing the counterclaim, *see* ER-941-45, 948-49.

dates of entry of summary judgment on claim and decision on counterclaim); PA51 ("[Petitioner's] compulsory counterclaim is not a core proceeding arising in a case under the Bankruptcy Code because it is not so closely related to [Respondent's] defamation claim that it must be resolved in order to determine the allowance or disallowance of his claim against her bankruptcy estate."); PA52 (noting an attenuated nexus between the claim and counterclaim); PA52 (noting differences between the nature and scope of allegations); PA53-54 (noting differences in proof and legal issues). Accordingly, *amici* submit that it does not implicate "public rights" and cannot be considered a "core" matter under 28 U.S.C. § 157.

CONCLUSION

Amici submit that 28 U.S.C. § 157 should be interpreted such that only those counterclaims that independently "arise under" the Code or that "arise in" a bankruptcy case may be "core" matters that can be finally adjudicated by a non-Article III bankruptcy court. If the Court concludes that a state-law counterclaim "arises in" a bankruptcy case since it is a response to a proof of claim, *amici* submit that such a counterclaim can be a "core" proceeding *only* where resolution of the counterclaim is intertwined with resolution of the allowance or disallowance of the claim itself. That is the only way in which a counterclaim can be viewed as being a matter of public rights. Here, the state-law tortious interference claim is a "non-core" proceeding that is merely "related to" the bankruptcy

case and over which *amici* submit the bankruptcy court lacked authority to issue a final judgment.

Respectfully submitted,

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AMICUS CURIAE BRIEF

Supreme Court, U.S.
FILED
OFFICE OF THE CLERK

No. 10-179

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On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF FOR THE CENTER FOR THE RULE OF LAW AS *AMICUS CURIAE* SUPPORTING THE RESPONDENT

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December 2010

WILSON-EPES PRINTING CO., INC – (202) 789-0096 – WASHINGTON, D. C. 20002

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Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF FOR THE CENTER FOR THE RULE OF LAW AS *AMICUS CURIAE* SUPPORTING THE RESPONDENT

INTEREST OF *AMICUS* [1]

The Center for the Rule of Law is a non-profit, educational institution of scholars and others interested in issues related to the rule of law. Issues of central concern to scholars at the Center include the preser-

[1] The parties to this case have filed with the Clerk of this Court written letters giving blanket consent to the filing of amicus briefs. This brief was not authored in whole or in part by counsel for any party, and monetary support for the preparation and submission of this brief has been provided entirely by *amicus curiae*, its members, and its counsel.

vation of impartial judicial processes and constitutional rules protecting property and individual rights. Affiliated scholars at the Center include long-time teachers and authors in the fields of constitutional and administrative law who have strong interests in promoting adherence to constitutional requirements and to rules that preserve predictable determination of legal rights (including their commitment to the fora most likely to provide consistent interpretation and effectuation of those rights). These interests are substantially affected by questions before this Court respecting the constitutionality of assigning to federal officials lacking essential attributes of Article III judges the power to decide questions traditionally within the preserve of state court judges or Article III federal judges.

SUMMARY OF ARGUMENT

The questions before the Court in this case are whether non-Article III bankruptcy judges are authorized by law to render final, binding decisions on state law private right claims and, if so, whether that authorization violates Article III of the Constitution. *Amicus* does not take a position on the terms of the statute itself, but if the law is read to grant the authority sought by petitioner, it should be held to violate the requirements of Article III.

Article III plainly and clearly declares that the "judicial power of the United States" is vested in a judiciary that is protected by certain specific guarantees of independence, notably including life tenure and irreducible compensation. U.S. Const., Art. III, § 1. This commitment of national judicial power to judges enjoying Article III's protections is set out in terms that contain no exceptions.

It was understood at the time, however, that the national judicial power did not comprehend every exercise of adjudicatory authority by the government. Matters presented in connection with the governance of federally-controlled territories, questions of military discipline or application of the laws of war to enemy combatants, and decisions on public rights (primarily, disposition of public property or public funds) were recognized as lying outside the scope of the national judicial power. This understanding was consistent with conceptions of judicial power embraced by Blackstone and Locke and with accepted practice at the time of the Constitution's framing. It also is consistent with interpretations of Article III by this Court from the early nineteenth century forward.

While non-Article III federal officers handled many matters and made many decisions, they did not enjoy final decisional authority over matters within the scope of the judicial power assigned by Article III. As this Court explained in *Crowell v. Benson*, 285 U.S. 22, 51 (1932), for such matters other officers may act essentially as adjuncts to Article III judges, but the Constitution does not permit them to render decisions that are final (subject only to ordinary appellate review). *Id.* at 51-65. This understanding of Article III's limits helped shape the array of administrative arrangements that has been adopted over more than three-quarters of a century.

Although the scope of one category of matters that fall outside the judicial power – administration of public rights – has been the subject of debate, it long has been clear that the broad run of state law tort claims is squarely within the class of disputes that would be categorized as involving private, not public, rights. State tort actions between private parties do

not constitute claims by or against the government, do not present issues whose resolution necessarily is subject to revision by the political branches (as is the case with certain obligations respecting public lands or public finance), and do not derive from federal law. Thus, they do not fit any conception of public rights. Claims respecting these state-created private rights must be decided by Article III judges. *See, e.g., Thomas v. Union Carbide Agricultural Prods. Co.*, 473 U.S. 568, 584 (1985); *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 69 (1982) (plurality op.); *Atlas Roofing Co. v. Occupational Safety and Health Review Comm'n*, 430 U.S. 442, 450, 458 (1977).

Non-Article III officers have been found constitutionally authorized to render decisions on such private law claims only where, first, the decision is essential to (integrally intertwined with) disposition of another matter that falls outside the scope of the judicial power *and*, second, the decision of the non-Article III officer is appropriately confined to assure that it fits *Crowell*'s conception of the administrative determination as advisory to an Article III court rather than as a final decision. *See Commodities Futures Trading Comm'n v. Schor*, 478 U.S. 833, 852-53 (1986). Whether even this limited commitment of authority to non-Article III officers is constitutional may be questioned, but the risks of expanding this category – risks to the integrity of the constitutional structure protected by Article III – cannot.

Bankruptcy law traditionally has operated within the limitations imposed by Article III. From 1800 to 1978, non-Article III personnel functioned as adjuncts to Article III judges, with no final decisional authority independent of the district court. Although

minor aspects of these adjuncts' authority varied over time, it was only in 1978 that Congress changed that central feature of the bankruptcy regime. This effort to confer final decisional authority on non-Article III bankruptcy judges was held unconstitutional in *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, *supra*. Subsequently, the law was reconstituted to again grant district court judges broad authority over bankruptcy judges' determinations. *See* Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 333.

The 1984 law, however, provides that the district courts can refer cases to the non-Article III bankruptcy judges. Bankruptcy judges then have authority to "hear and determine" certain "core" matters that become final decisions of the court, but they are only authorized to "submit proposed findings of fact and conclusions of law to the district court" for other, "non-core" matters. *See* 28 U.S.C. § 157(b), (c). Interpretation of this provision is disputed. However, reading the provision as granting bankruptcy judges final decisional authority over state law tort claims would conflict with the commands of Article III.

Precedents of this Court dealing with settings in which bankruptcy trustees sought to recover avoidable preferences from claimants against the bankrupt's estate – raising matters that are at the very heart of the bankruptcy process and also are necessarily implicated in the nature of the claims filed – do not support conferring decisional authority over the state law tort claims at issue here. *Katchen v. Landy*, 382 U.S. 323 (1966), and *Langenkamp v. Culp*, 498 U.S. 42 (1990), addressed the right to jury trial (an issue related to the constitutional question presented here). Both *Katchen* and *Langenkamp* involved claims

by individuals who allegedly had received avoidable preferences (through self-dealing) and who then sought distributions from the bankrupt's estate. In these circumstances, the distribution of assets in the bankrupt's estate depended directly on disposition of the claims those parties filed against the estate and the preference assertions against the claimants. Although the preference assertions could have been brought by the respective bankruptcy trustees as separate suits, resolving them together with the claims they offset fit the traditional scope of bankruptcy proceedings.

The facts of this case are very different from *Katchen* and *Langenkamp*. This case presents two private state law tort claims: neither concerns preference claims; neither depends directly on the other; and neither was essential to disposition of the assets of the bankrupt's estate to other claimants in the bankruptcy proceeding. Unlike the limited waiver of jury trials approved in those cases, expanding the class of determinations subject to decision by non-Article III bankruptcy judges to cover this case would greatly increase the number of settings in which private law rights would be subject to disposition outside of normal judicial proceedings. Indeed, it is difficult to imagine administrative programs that could not sweep a broad array of private law claims into their net. Such an expansion would threaten to unravel Article III's protections.

Opposition to a straight-forward application of Article III's requirements rests in part on an assumption that this would undermine the efficiency of the bankruptcy process, leading to increased cost and delay. *See, e.g.*, Brief for *Amicus Curiae* United States, at 16. Concerns for any impact on the

administrative efficiency of the bankruptcy process, however, are easily exaggerated. After all, the bankruptcy process has functioned for almost two centuries without placing authority over state law tort claims outside the Article III courts. In all events, even well-grounded efficiency concerns do not justify departing from constitutional command.

ARGUMENT

I. ARTICLE III'S REQUIREMENTS APPLY TO ALL FINAL DECISIONS WITHIN "THE JUDICIAL POWER" OF THE UNITED STATES

A. Article III's Language and Contemporary Understanding Are Clear and Unexceptional

The framers of the Constitution self-consciously created a system in which judicial power was vested in a judiciary insulated from the political branches. Article III, § 1 declares that "The judicial Power of the United States shall be vested in one supreme Court and such inferior courts as Congress may from time to time ordain and establish." It then commands that "The Judges, of both the supreme and inferior Courts, shall hold their Offices during good Behaviour" and shall receive compensation which cannot be diminished.

The protections of life tenure and irreducible pay were important considerations to the framers. Alexander Hamilton put the case bluntly in Federalist No. 78:

> The standard of good behavior for the continuation in office of the federal magistracy, is certainly one of the most valuable of the modern improvements in the practice of government. In a

> monarchy, it is an excellent barrier to the despotism of the prince; in a republic it is a no less excellent barrier to the encroachments and oppressions of the representative body. And it is the best expedient which can be devised in any government, to secure a steady, upright, and impartial administration of the laws.

THE FEDERALIST NO. 78, at 503 (Edward Meade Earle ed., 1937). This was not merely a throw-away line, but the focus of much of Hamilton's argument in favor of the Constitution's arrangements respecting the judicial branch. Hamilton trumpeted the independence that such arrangements produced as especially vital when courts might have the necessity to decide that the legislative branch had overstepped its constitutional bounds, *id.* at 505-508, but also found them advisable in securing the independence of judicial decisions in other matters as well, *id.* at 509-11; THE FEDERALIST NO. 79, at 512-13 (Edward Meade Earle ed., 1937).

Nothing in the text of Article III suggests any exceptions to these requirements. Nothing in the text suggests the possibility that Congress might constitutionally choose to create courts whose judges exercise some of the federal judicial power without the specific attributes of independence mentioned in the Article's first section. There is no qualifying language saying that these arrangements will obtain unless Congress (or Congress and the President in concert) deems a different structure necessary. Such a qualification would be wholly at odds with the evident meaning and purpose of the provisions in Article III.

This Court's decisions repeatedly have emphasized the deep historical roots of the provisions for life tenure and irreducible pay and the importance of

these protections to judicial independence. *See, e.g.*, *United States v. Will*, 449 U.S. 200, 217-21 (1980); *United States ex rel. Toth v. Quarles*, 350 U.S. 11, 16 (1955); *O'Donoghue v. United States*, 289 U.S. 516, 531-34 (1933). Articulating the starting point for another inquiry into the consistency of the legal regime governing bankruptcy determinations with the mandates of Article III, Justice Brennan, writing for the plurality in *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982), declared:

> [O]ur Constitution unambiguously enunciates a fundamental principle–that the "judicial Power of the United States" must be reposed in an independent Judiciary. It commands that the independence of the Judiciary be jealously guarded, and it provides clear institutional protections for that independence.

Id. at 60. That again should be common ground for the inquiry at bar.

B. Academic Suggestions of Exceptions to Article III's Requirements Mischaracterize the Scope of Federal Judicial Power

In spite of the clear command of Article III respecting the institutional protections that must be extended to federal officials exercising the judicial power of the United States, there has been confusion – especially within the academic community – over the occasions in which adjudicatory functions have been, and constitutionally may be, committed to other officials. Several legal scholars have concluded that Article III must be read to include qualifications because a literal application of the Constitution

would conflict with practices they believe should not be disturbed.

Professor Pfander, for example, announced that, "despite the importance of these provisions to the framing of the Constitution and their centrality to founding-era notions of judicial independence and the separation of powers, Congress has often assigned disputes that appear to fall within the scope of the federal judicial power to . . . tribunals whose judges lack salary and tenure protections." James Pfander, *Article I Tribunals, Article III Courts, and the Judicial Power of the United States*, 118 Harv. L. Rev. 643, 646 (2004). He sums up the academic literature trying to make sense of the use of non-Article III tribunals by asserting that "[n]early everyone agrees that Article III defies literal interpretation." *Id.*

Professor Fallon (who is among the relatively small number of authorities cited by Pfander in support of that proposition)[2] also starts with acceptance of the clarity of Article III's commands before declaring that they cannot be taken at face value:

> By nearly universal consensus, the most plausible construction of [the Constitution's] language would hold that if Congress creates any adjudicative bodies at all, it must grant them the protections of judicial independence that are contemplated by article III. . . . Today, the familiar roles of legislative courts and especially of administrative agencies render a return to 'article III literalism' virtually unthinkable.

[2] Curiously, Professor Pfander cites more authorities who *disagree* with the conclusion he says "[n]early everyone agrees" with than who are in accord with it. *See* 118 Harv. L. Rev. at 646-47 nn. 2-10.

Richard H. Fallon, Jr., *Of Legislative Courts, Administrative Agencies, and Article III*, 101 Harv. L. Rev. 915, 916-17 (1988) (citations omitted).

What makes the notion of following the Constitution's commands as plainly written "unthinkable" is the array of settings in which non-Article III officers have been granted authority to decide matters that might in other circumstances have come before courts constituted in conformity to Article III. As Professors Fallon and Pfander point out, Congress, from early in the republic's history, has assigned executive officials, non-Article III tribunals, and administrative agencies tasks that look very similar to adjudication and that, if put in dispute in a "case or controversy," might indeed fall within the judicial power of the United States.

That particular decisions *might* be within the judicial power in other circumstances, however, does not mean that they *are* within that power when assigned to others nor does it mean that Congress is free to decide when to assign a matter to a non-Article III officer. The conjectures of scholars who write in support of diluting Article III's clear meaning depend critically on acceptance of one or both of those conclusions.

The historical record supports a very different conclusion: that non-Article III officers traditionally have been asked to render judgments either that are not on matters within the judicial power of the United States or that do not have finality until endorsed by judges protected by the special guarantees set forth in Article III. This Court's decisions are overwhelmingly in keeping with that conclusion.

C. The Federal Judicial Power Does Not Extend to Matters of Local, Territorial or Similar Non-National Law Enforcement, of Military Justice, or of Public Rights

The plurality opinion in *Marathon* accurately summarized this Court's prior decisions respecting appropriate delegation of adjudicatory authority to decision-makers who lack Article III's protections. Three headings make up this list.

First, there are determinations of matters that lie outside the national sphere – and, hence, outside the judicial power of the United States – because they are local disputes over which the Congress exercises authority in the nature of a lesser sovereign, on par with a state or local government, rather than in its capacity as legislature for the national government. That was the rationale of Chief Justice Marshall in *American Ins. Co. v. Canter*, 26 U.S. (1 Pet.) 511, 546 (1828), with respect to territorial courts' non-Article III status. The same reasoning supported decision that local matters respecting the District of Columbia could be tried in courts set up in the nature of state or local courts, though under Congress' authority to regulate affairs of the District. *Palmore v. United States*, 411 U.S. 389, 406-10 (1973). Similarly, the disposition of tribal matters has been held to be outside the purview of the federal judicial power, as Native American tribes are independently sovereign. *See Wallace v. Adams*, 204 U.S. 415, 422 (1907).

In all of these instances, a claim involving federal law could be presented and disputed such that federal appellate jurisdiction could attach – for example, to review a question of jurisdiction. *See, e.g., In re Moran*, 203 U.S. 96 (1906). However, an initial

determination of claims based on law applicable only in particular enclaves or under the law of another sovereign – not under national, federal law or under the grant of federal diversity jurisdiction over conflicts between residents of different states – would not be within the judicial power of the United States. This view is consistent with the way eighteenth and nineteenth century jurists and scholars thought about the scope of a jurisdiction's judicial power. *See, e.g.*, Caleb Nelson, *Adjudication in the Political Branches*, 107 Colum. L. Rev. 559, 575-77 (2007); Craig Stern, *What's a Constitution Among Friends? – Unbalancing Article III*, 146 U. Pa. L. Rev. 1043, 1068 (1998).

Second, military tribunals such as courts-martial or panels for trying foreign enemy combatants under the laws of war were not considered to be within the judicial power of the United States. *See Dynes v. Hoover*, 61 U.S. (20 How.) 65, 79 (1857). While there is debate today about whether these proceedings should be thought to be subject principally to the executive's authority over the military or the legislature's, the proceedings, though adjudicatory, were not thought to be within the realm of law committed to national courts and Article III judges. *See, e.g.*, *Johnson v. Eisentrager*, 339 U.S. 763, 786-87 (1950); *Ex parte Quirin*, 317 U.S. 1, 40-41 (1942); Curtis Bradley & Jack Goldsmith, *The Constitutional Validity of Military Commissions*, 5 Green Bag 2d 249 (2002).

Third, matters pertaining to the disposition of public property or public funds were thought to be outside the scope of judicial power. Two reasons supported placing these claims outside Article III's reach. One was that final resolution of these tended to be subject to discretionary authority in the politi-

cal branches regarding ultimate payment or disposition of property; that removed them from matters that the courts could finally resolve, making the judicial decision in some sense merely advisory, hence, not properly matters for strictly judicial disposition. *See, e.g., Muskrat v. United States*, 219 U.S. 346, 352-62 (1911); *Gordon v. United States*, 69 U.S. (2 Wall.) 561 (1865); *United States v. Ferreira*, 54 U.S. (13 How.) 40, 52 (1851). The other was that these claims did not involve matters of private right but instead presented claims by or against the public. Those matters then were viewed as not within the ambit of the judicial authority, either following the traditional definition of what matters are judicial or as matters withdrawn from that sphere by virtue of sovereign immunity. *See, e.g., Northern Pipeline Construction Co. v. Marathon Pipe Line Co., supra*, at 69 (plurality op.); *Atlas Roofing Co. v. Occupational Safety and Health Review Comm'n*, 430 U.S. 442, 450, 457-58 (1977); *Ex parte Bakelite Corp.*, 279 U.S. 438, 451 (1929); *Murray's Lessee v. Hoboken Land & Improvement Co.*, 59 U.S. (18 How.) 272, 283 (1856); Nelson, *supra* at 577-89. This is the category of cases referred to in *Marathon*, as it has been since this Court's decision in *Murray's Lessee*, as involving "public rights."

Delineation of the class of cases properly referred to under this heading has been a matter of some debate. *See, e.g., Granfinanciera, S.A. v. Norberg*, 492 U.S. 33, 66-70 (1989) (Scalia, J., concurring); *Commodities Futures Trading Comm'n v. Schor*, 478 U.S. 833, 851-56 (1986); *Thomas v. Union Carbide Agricultural Prods. Co.*, 473 U.S. 568, 587-89 (1985); *id.* at 596-99 (Brennan, J., concurring). The scope of this category is addressed further below.

What should be clear is that the public rights cases, like cases in the other categories set forth above, describe matters that are not within the federal judicial power. That does not mean that no case could be designed to present a conflict regarding the general subject in a manner that could be within the judicial power. *See, e.g., Murray's Lessee, supra* at 284 ("matters [] involving public rights . . . may be presented in such form that the judicial power is capable of acting on them"). As Professor Nelson explains particularly clearly, however, under the framework of rights understood by jurists and theorists whose work influenced the framing of the Constitution, most of all Blackstone and Locke, public rights were within the peculiar province of the political branches of government and were not judicially cognizable in the same way as private rights. *See* Nelson, *supra* at 566-72. *See also* Ann Woolhandler, *Public Rights, Private Rights, and Statutory Retroactivity*, 94 Geo. L.J. 1015, 1020-22 (2006).

Recognition of occasions in which non-Article III officers have been given decisional authority over matters that lie outside the ambit of national judicial power (as understood at the time of the Constitution's framing and as repeatedly reaffirmed since then) does not, thus, establish a list of *exceptions* to Article III. Instead, it is consistent with the Constitution's vesting of the national judicial power – and *only* that power – in the Article III courts.[3] Consideration of the three categories referenced in *Marathon* helps define the limits of the power assigned in Article III,

[3] To be sure, state courts were thought capable of exercising authority over questions that might be contested in the federal courts. The role of state courts is discussed *infra*.

just as this Court's exposition of the meaning of the terms "case or controversy" elsewhere does.

Academic criticism of this Court's treatment of these categories as failing to establish a coherent theory of judicial power, *see, e.g.*, Fallon, *supra* at 948, misses the point. Although there may be some question about the outer contours of any category, the categories describe matters that were understood not to be within the scope of national judicial power in the first place. That should be a sufficiently coherent basis for judicial decisions. Unlike academic writing, this Court's task is not to establish an overarching theory of judicial power, but to implement constitutional command, a task that fits well with the Court's decisions respecting Article III's scope.

D. Administrative Agencies' Authority Traditionally Has Not Encompassed Final Decision on Matters within the Judicial Power

Although scholarly commentary has evinced concern that a straight-forward interpretation of Article III would invalidate large swaths of the now firmly established administrative state, virtually none of the decisions committed to administrative officials (who do not enjoy Article III's protections) is at risk. Vast stretches of the landscape associated with the administrative state fall into one of three categories that do not call the terms of Article III into question.

First, the overwhelming majority of administrative actions are not adjudicatory in nature. Officials collect fees, process requests, forward information, buy goods and services, keep accounts, contract for buildings and maintain them, analyze data, conduct

research, support personnel (military and civilian) at home and abroad, and do much more that defies description as adjudication.

Second, decisions that are adjudicatory in some sense primarily (indeed, almost entirely) consist of determinations on matters such as benefits, licenses, taxes, and other matters falling squarely within the category of public rights issues that lie outside the scope of the judicial power. *See, e.g.*, Ronald A. Cass, *Allocation of Authority within Bureaucracies: Empirical Evidence and Normative Analysis*, 66 B.U. L. Rev. 1, 11 n. 50 (1986) (Social Security benefits adjudications comprise 95 percent of formal administrative adjudications in federal government).

Third, insofar as the issues decided by administrators appear to fall within the realm of the judicial power, those decisions are not final in the same sense as a judicial determination until confirmed by a judge appointed in conformity with Article III. The classic exposition is *Crowell v. Benson*, 285 U.S. 22 (1932), which found that lack of finality on matters within the judicial power (as well as on "jurisdictional facts" critical to determination whether a matter *is* within the judicial power) preserved the constitutional legitimacy of an administrative scheme. *Id.* at 51-65 (approving law respecting employment-related compensation of longshoremen). *Crowell* analogized the role of the agency there to that of a special master whose determinations, even where there is some weight given to them, "are essentially of an advisory nature," assisting the Article III court that finally decides matters. *Id.* at 51.

This Court repeatedly has invoked *Crowell*'s reasoning in deciding whether other statutory arrangements provide constitutionally sufficient

review by an Article III judge of critical determinations respecting private rights. *See, e.g., United States v. Raddatz*, 447 U.S. 667, 682-83 (1980) (upholding use of federal magistrates for non-final dispositions of criminal cases); *Northern Pipeline Construction Co. v. Marathon Pipe Line Co., supra*, 458 U.S. at 77-86 (striking down commitment of final authority over bankruptcy determinations to non-Article III judges). Although *Crowell*'s distinction between "jurisdictional facts" and other facts has proved elusive, this Court has continued to invoke Chief Justice Hughes' basic insight that non-Article III tribunals can provide a first level determination but not a final decision on matters within the judicial power of the United States. *See, e.g., Commodities Futures Trading Comm'n v. Schor, supra*, 478 U.S. at 852-53; *Thomas v. Union Carbide Agricultural Prods. Co., supra*, 473 U.S. at 586-87; *Atlas Roofing Co. v. Occupational Safety and Health Review Comm'n, supra*, 430 U.S. at 450.

II. FINAL DECISION OF STATE LAW TORT CLAIMS CANNOT BE COMMITTED TO NON-ARTICLE III FEDERAL OFFICERS

A. State Law Tort Claims Are Private Rights Subject to Article III's Mandates

The dispute in this case involves state law tort claims that are quintessential private rights. Although they have been swept into the ambit of a bankruptcy proceeding, the claims at issue are state law tort claims. Indeed, in this case, the matter in dispute is a state law tort claim (tortious interference with an expectancy of a gift) purportedly asserted as a counterclaim to another state law tort claim (defa-

mation).[4] In other words, this case presents the question of whether Article III can be displaced in adjudicating rights among private parties where one private state law right is asserted in opposition to another private state law right.

State law tort claims, of course, can be heard by state officials who do not share Article III's protections. Nothing in the Constitution purports to impose those same requirements on state judges as it does on judges exercising the judicial power of the United States.

The national judicial power, however, expressly extends to such claims when they arise between citizens of different states. U.S. Const., Art. III, § 2. In that circumstance, at the very least, there can be no thought that controversies rooted in state private law claims are assignable for final decision by non-Article III officers, "subject only to ordinary appellate review." *See Thomas v. Union Carbide Agricultural Prods.*, *supra*, 473 U.S. at 584 (describing holding in *Marathon*, *supra*). As this Court said in *Atlas Roofing*, *supra*:

> Our prior cases support administrative fact-finding in only those situations involving "public rights," *e.g.*, where the Government is involved in its sovereign capacity under an otherwise valid statute creating enforceable public rights. Wholly private tort, contract, and property cases, as well

[4] The degree to which the state law tort claims were actually before the bankruptcy court is a matter of dispute. *See Marshall v. Stern (In re Marshall)*, 600 F.3d 1037, 1044 (9th Cir. 2010); *id.* at 1065 (Kleinfeld, J., concurring). Under the reading most favorable to petitioner, the case presents two competing state law private rights claims.

> as a vast range of other cases, are not at all implicated.

430 U.S. at 458. The Court also stated that "[i]n cases which do involve only 'private rights,' this Court has accepted factfinding by an administrative agency, without intervention by a jury, only as an adjunct to an Art. III court." *Id.* at 450 n. 7.

This does not mean that there can be *no* involvement of non-Article III decision-makers in adjudication of private rights. Notably, *Schor* rejected the contention that federalism concerns respecting the division of state and national powers (as opposed to considerations relevant to the separation of powers within the national government) "absolutely preclude any adjudication of state law claims" by non-Article III federal officers. *Commodities Futures Trading Comm'n v. Schor*, *supra*, 478 U.S. at 858. That rejection was based in part on the perceived misfit between the theory and the assertion and in part on the Court's view that there was *some* scope for determinations of private rights by non-Article III officers.

Although *Schor* departed from prior decisions in its description of the category of public rights, *see Granfinanciera, S.A. v. Norberg*, *supra*, 492 U.S. at 66-70 (Scalia, J., concurring), the Court's opinion emphasized that non-Article III adjudication of private, state law claims was constitutional only because it had certain characteristics that brought it within *Crowell*'s ambit of adjunct, not final, determination:

> The [statutory] scheme . . . hews closely to the agency model approved by the Court in *Crowell v. Benson*. The CFTC, like the agency in *Crowell*, deals only with a "particularized area of law,"

> whereas the jurisdiction of the bankruptcy courts found unconstitutional in *Northern Pipeline* extended to broadly "all civil proceedings arising under title 11 or arising in or *related to* cases under title 11." . . . CFTC orders, like those of the agency in *Crowell*, but unlike those of the bankruptcy courts under the 1978 Act, are enforceable only by order of the district court. CFTC orders are also reviewed under the same "weight of the evidence" standard sustained in *Crowell*, rather than the more deferential standard found lacking in *Northern Pipeline*. The legal rulings of the CFTC, like the legal determinations of the agency in *Crowell*, are subject to *de novo* review. Finally, the CFTC, unlike the bankruptcy courts under the 1978 Act, does not exercise "all ordinary powers of district courts" . . .

478 U.S. at 852-53 (citations omitted).

Schor did expand the scope of authority for non-Article III officers, perhaps beyond what best fits constitutional text and historical understanding, *see, e.g.*, Fallon, *supra*, at 917, but the Court nonetheless took pains to circumscribe the decision. The Court's opinion makes clear that it would not approve even initial decision of private right state law claims except in limited circumstances and would not approve any final decision of a private state law claim by non-Article III officers.

The Court underscored that point in *Granfinanciera v. Norberg*, *supra*, in deciding the closely related question of the consistency of an adjudicative process with Seventh Amendment jury-trial rights. *Id.*, 492 U.S. at 53. The Court cautioned that decisions approving fact-finding by an administrative agency

as an adjunct to an Article III court "should not be taken to mean that Congress may assign at least the initial factfinding in all cases involving controversies entirely between private parties to administrative agencies or other tribunals not involving juries, so long as they are established as adjuncts to Article III courts." *Id.*, 492 U.S. at 55 n. 10. Quoting from the plurality in *Marathon*, the Court reiterated that private law claims subject to suits at law, equity, or admiralty "lie at the 'protected core' of Article III judicial power." 492 U.S. at 56.

This Court's decisions clearly require judges who enjoy Article III's protections, not other federal officers, to render final judgment on state private law claims. Because state law tort claims of the sort at issue here lie squarely within that set of matters, their disposition must be confided to Article III judges.

B. Bankruptcy Law Historically Has Committed Final Decision of Private Law Claims to Article III Judges

Nothing in the nature of bankruptcy law, in the historical structure of bankruptcy adjudications, or in this Court's precedents regarding bankruptcy law alters the analysis above.

Bankruptcy adjudications historically have proceeded as matters within the full authority of Article III judges, with other officers serving only as adjuncts to the judges. *See, e.g.*, Tuan Samahon, *Are Bankruptcy Judges Unconstitutional? An Appointments Clause Challenge*, 60 Hastings L.J. 233, 236-40 (2008). The officers – at various times labeled commissioners, registers, referees, or judges – performed a variety of tasks, both ministerial and judgmental, but they

were never given final authority to decide matters of private right. *Id.* The bankruptcy officers expressly served as adjuncts to district court judges who are appointed in conformity to Article III, and the officers' decisions were always subject to review by the district court. *See* Act of July 1, 1898, ch. 541, § 38, 30 Stat. 544, 555. This pattern obtained over repeated iterations of bankruptcy law spanning more than 175 years. It was broken only by the 1978 revision of the bankruptcy law that was declared unconstitutional in *Marathon, supra.*

The assignment to non-Article III bankruptcy officers of final adjudicatory authority over private rights embedded in state tort law would be at odds not only with the text of the Constitution and the history of bankruptcy law – it also would be at odds with the decisions of this Court respecting the ambit of Article III authority, both in cases directly concerning that question and in disposition of Seventh Amendment issues on analogous grounds. *See Granfinanciera v. Norberg, supra,* at 55-56; *Commodities Futures Trading Comm'n v. Schor, supra,* 478 U.S. at 852-53; *Thomas v. Union Carbide Agricultural Prods. Co., supra,* 473 U.S. at 586-87; *Atlas Roofing Co. v. Occupational Safety and Health Review Comm'n, supra,* 430 U.S. at 450.

The Solicitor General's *amicus* brief states that interim rules adopted by the various circuits of the court of appeals, all based on the rule suggested by the Director of the Administrative Office of the Courts following *Marathon*, were "uniformly upheld against constitutional challenge by the court of appeals." Brief for *Amicus Curiae* United States, at 7. Although accurate if read narrowly, that statement cannot support inference that the court of appeals

uniformly has resolved (and rejected) the constitutional challenge presented in this case.

Virtually all of the cases cited by the Solicitor General focus on matters such as the permissibility of judicial adoption of a bankruptcy rule or the existence of jurisdiction in the district court following enactment of the Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549, and preceding enactment of the Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 333. *See, e.g., Braniff Airways, Inc. v. Civil Aeronautics Bd.*, 700 F.2d 214, 215 (5th Cir.) (*per curiam*), *cert. denied*, 463 U.S. 1208 (1983) (relying on 27 B.R. 231 (N.D. Tex. 1983)); *White Motor Corp. v. Citibank, N.A.*, 704 F.2d 254, 263 (6th Cir. 1983); *Stewart v. Stewart*, 741 F.2d 127, 131-32 (7th Cir. 1984). They generally do not address the constitutionality of a bankruptcy judge rendering final decision on private rights, the issues that are presented in the instant case.

Indeed, to the extent the cases cited by the Solicitor General do look to the matters at hand, the circuit courts mainly suggested that the rule was constitutional only insofar as it reverted to making the bankruptcy judge an adjunct to the Article III district court judge and did not grant final authority to the bankruptcy judge. *See, e.g., Salomon v. Kaiser*, 722 F.2d 1574, 1580 (2d Cir. 1983) ("'even in traditional bankruptcy cases, the district courts may hold a hearing and receive evidence in cases first adjudicated by the bankruptcy court. The district court need give no deference to the bankruptcy judge's factual findings or interpretations of the law,'" quoting *White Motor Corp. v. Citibank, supra*); *White Motor Corp. v. Citibank, supra*, at 263 ("The interim

rule does not violate the Constitution because the district courts retain primary jurisdiction over all bankruptcy proceedings. . . . The district courts retain control and primary responsibility for the conduct of bankruptcy proceedings."); *Stewart v. Stewart*, *supra*, at 132 ("The Interim Rule adopted by the district courts establishes a system of bankruptcy adjudication whereby the bankruptcy judges act as adjuncts of the Article III district courts. . . . The bankruptcy judges act as subsidiaries to and only in aid of the district courts by carrying on preliminary procedures and proposing decisions for adoption by the district court. The ultimate adjudicatory determination is reserved to the district judge. The Interim Rule sufficiently ensures that Article III powers are exercised by Article III judges . . ." (citations omitted)).

Far from asserting the constitutional propriety of conferring final decisional authority on bankruptcy judges with respect to private rights created by state law, the cases cited by the Solicitor General propose just the opposite: that the interim rule, and by extension the 1984 law, would be constitutional only insofar as they resist precisely the assignment of authority advocated by petitioner in this case. Subsequent court of appeals decisions likewise have concluded that conferring final decisional authority on bankruptcy judges, even on core bankruptcy issues, would violate Article III for any matter that would have been subject to a suit at law. *See*, *e.g.*, *Germain v. Connecticut National Bank*, 988 F.2d 1323, 1328-32 (2d Cir. 1993); *In re Clay*, 35 F.2d 190, 192-95 (5th Cir. 1994); *Piombo Corp.v. Castlerock Properties (In re Castelrock Properties)*, 781 F.2d 159, 160 (9th Cir. 1986); *In re Parklane/Atlanta Joint Venture*, 927 F.2d 532 (11th Cir. 1991). The Fifth Circuit's opinion in *Clay* typifies these decisions in adding that devolu-

tion of authority to a non-Article III bankruptcy judge cannot be saved by asserting that bankruptcy proceedings are at their core matters of "public right." *In re Clay*, *supra*, at 194 ("[B]ankruptcy law . . . provides process, procedures, and a forum, but does not (as would a public regulatory scheme) implement policy choices beyond the confines of the cases brought to it.").

In short, to the extent decisions of the court of appeals are thought to provide helpful guidance on this matter, they support the conclusion that non-Article III bankruptcy judges cannot constitutionally be given final decisional authority respecting state private law claims.

C. Filing Non-dischargeability Petition and Proof of Claim Did Not Constitute Consent to Decision of State Law Tort Claims by Bankruptcy Judge

The actions at issue in this case do not amount to either consent to the exercise of constitutionally suspect authority over disposition of a private state law tort claim or waiver of objections to such an exercise of authority. The facts in this case differ substantially from cases in which either consent or waiver may have played a role in the Court's disposition of contentions respecting a process' conformity to related constitutional requirements. For example, in *Commodities Futures Trading Comm'n v. Schor*, *supra*, the complaint about the administrative agency's exercise of authority over a state law claim was advanced by William Schor, the party who had invoked the agency's authority in the first instance, who had resisted trial of the state law claim in district court (asserting that the administrative agency could handle the matter full well), and whose

insistence on the administrative forum had led to the voluntary dismissal of the suit in favor of a counterclaim in the administrative process. *See id.*, at 837-38.

Katchen v. Landy, 382 U.S. 323 (1966), began when Louis Katchen filed a claim in a bankruptcy proceeding (having already distributed to himself assets of the soon-to-be-bankrupt business), and the trustee in bankruptcy responded by asserting that Katchen had received an avoidable preference from the bankrupt enterprise. In that context, the Court found that Katchen did not have a right to a jury trial, even though he would have if he had merely resisted an independent effort by the trustee to collect the preference. *Id.* at 335-40. As the Court said, the essence of the equity jurisdiction of the bankruptcy court was the allowance and disallowance of claims, and the avoidable preference question was central to that process: the bankruptcy court could not decide if Katchen had a right to share in the estate until it decided the preference issue. *Katchen*, however, does not address (much less dispose of) the Article III issue presented in this case, nor does it establish that every claim filed in a bankruptcy action constitutes consent to the use of non-Article III proceedings for disposition of all related issues.

This Court followed *Katchen* in *Langenkamp v. Culp*, 498 U.S. 42 (1990), another case in which a bankruptcy claimant assertedly had received an avoidable preference which the trustee sought to recover. Again, the Court decided that filing the claim caused Culp and associated claimants to forfeit the right to a jury trial, though, as in *Katchen*, they would have retained the right had they simply resisted a legal action by trustee Langenkamp to

collect amounts received. As in *Katchen*, the claims and counterclaims in *Langenkamp* went to the heart of the bankruptcy processes of determining and distributing assets of the bankrupt's estate and the party contesting application of bankruptcy procedures had plainly sought to invoke just those procedures to adjudicate a specific monetary claim against the estate. In neither case were the claims and counterclaims presentable as private state law rights independent of the bankruptcy.

This case cannot be resolved on the basis of decisions such as *Katchen* and *Langenkamp* concerning adjudication of avoidable preference issues. Whether Pierce Marshall's filings of a non-dischargeability complaint and subsequently a proof of claim with the bankruptcy court constituted in some respect the filing of a claim in the bankruptcy action – an issue on which the judges of the court of appeals disagreed, *see Marshall v. Stern (In re Marshall)*, *supra*, 600 F.3d at 1044; *id.* at 1065-67 (Kleinfeld, J., concurring) – those filings were significantly different from the claims filings in *Katchen* and *Langenkamp*. Marshall's filings did not specify an amount sought, claimed no preference (and he had received no preference), and did not affect other claimants' rights. *See id.* at 1045 (bankruptcy court, pursuant to settlement between Vickie Lynn Marshall and creditors, had discharged Vickie Lynn Marshall's other pre-existing debts prior to trial and decision on adversary issues between her and Pierce Marshall); *id.* at 1068 (Kleinfeld, J., concurring). The majority of the panel below concluded that the non-dischargeability petition and proof of claim constituted the assertion of a claim in the bankruptcy proceeding. *Id.* at 1044-45. In contrast, Judge Kleinfeld, concurring, saw the complaint merely as an effort to obtain a

ruling that any future defamation claim would be unaffected by the bankruptcy process, with the proof of claim filed as a measure that was legally necessary in support of the complaint (to preserve the contemplated state law claim). *Id.* at 1068 (Kleinfeld, J., concurring).

However the filings are characterized, two things should be clear. First, the filings by Pierce Marshall were a far cry from the claims asserted by Louis Katchen or the Culps in relation to the central functions of bankruptcy. *Cf. Katchen v. Landy*, *supra*. Unlike Mr. Katchen, resolution of Pierce Marshall's filings did not affect the returns available to anyone in the bankruptcy proceeding apart from the one person who was the potential defendant in the contemplated defamation action, Vickie Lynn Marshall. *Id.* at 1045 ("[T]he bankruptcy court discharged Vickie Lynn Marshall's pre-existing debts and caused the property remaining in the bankruptcy estate to be revested in her" before deciding on the state law claims.).

Second, those filings should not be treated as implicitly consenting to the authority of the bankruptcy judge to enter a final decision on state law private rights claims or waiving objections to the constitutionality of such a decision. In sharp contrast to Mr. Schor, for instance, Pierce clearly objected to the consideration and decision of substantive matters regarding the state law claims - including both the defamation claim and the tortious interference claim – by the bankruptcy judge. *See Marshall v. Stern (In re Marshall)*, *supra*, 600 F.3d at 1045; *id.* at 1065-67 (Kleinfeld, J., concurring).

If filing a proof of claim is necessary to preserve rights in the event of an eventual recovery on state

law claims in another court, construing that filing as consent to whatever procedure – even one that violates constitutional strictures – is used in the bankruptcy proceeding substitutes bootstrapping for analysis. *See, e.g., Germain v. Connecticut National Bank, supra,* 988 F.2d at 1330 ("[N]either precedent nor logic supports the proposition that either the creditor or the debtor automatically waives all right to a jury trial whenever a proof of claim is filed."). If the counterclaim filed in response to the proof of claim is necessary to preserve correlative rights (though in this case, that is not clearly so), it takes a compound form of bootstrapping to construe the initial filing as agreement to having whatever state law private rights claims are presented in opposition finally determined by the bankruptcy court. The metaphysical contortions needed to achieve "consent" in this context are more redolent of theology than of law.

Ultimately, the threat of expanding the concept of consent or waiver to cover this case is an unraveling of Article III's protections. It is difficult to construct scenarios in which there could not be a similar contention of waiver once a party is drawn into an administrative process, despite the Hobson's choice presented to those who must either participate in the process or forfeit valuable claims.

D. Constitutional Command Cannot Be Subordinated to Interests in Efficient Process

As a rule, this Court construes statutes whenever possible to avoid constitutional invalidity. *See, e.g., United States ex rel. Attorney General v. Delaware & Hudson Co.,* 213 U.S. 366, 408 (1909) ("where a statute is susceptible of two constructions, by one of which grave and doubtful constitutional questions

arise and by the other of which such questions are avoided, our duty is to adopt the latter."). While that is not always possible, consistent with a fair reading of the text, it certainly is the better choice when the text leaves that option open.

An opposed set of arguments supports interpreting statutory provisions in ways that might conflict with constitutional command but that enhances or preserves other values, such as efficient administration of the law. *See, e.g.*, Brief for *Amicus Curiae* United States, at 16. In this case, the Court has been urged to allow a non-Article III bankruptcy judge to render final decision on a state law tort claim (a quintessential claim of private right) in order to "avoid significant delay and inefficiency." *Id.*

It is far from evident that a decision hewing to the established understanding and clear textual command of Article III would engender the costs that the Solicitor General fears. (Rejecting a similar argument, the court of appeals noted that those opposed to strengthening district court authority in bankruptcy "trumpet efficiency, but we hear a kazoo, at best." *In re Clay*, *supra*, 35 F.3d at 195.) A variety of mechanisms is available to permit bankruptcy judges to function as adjuncts to the district courts without creating administrative quagmires. It is, however, up to the political branches, not this Court, to select the best mechanism.

In all events, the cost of finding alternatives that fit more readily within the strictures of the Constitution is not a consideration that should guide this Court. As the Court has said in another context:

> [T]he fact that a given law or procedure is efficient, convenient, and useful in facilitating

> functions of government, standing alone, will not save it if it is contrary to the Constitution. Convenience and efficiency are not the primary objectives – or the hallmarks – of democratic government . . .

INS v. Chadha, 462 U.S. 919, 944 (1983).

Many of the Constitution's provisions – two separate houses of Congress selected from different constituencies for different terms, the Electoral College, protections of individuals' rights against self-incrimination and to trial by jury, for examples – are designed not to promote efficiency, narrowly conceived, but to serve broader goals the Framers deemed worthy of the added cost and inconvenience. *See, e.g.*, THE FEDERALIST NO. 51, at 337 (Edward Meade Earle ed., 1937) (Madison) ("A dependence on the people is, no doubt, the primary control on government; but experience has taught mankind the necessity of auxiliary precautions."); *id.*, NO. 78, at 505 (Hamilton). If the political branches are free to elide constitutional commands whenever that seems more efficient, there will be no limitation to the revisions that might be made to our most basic governing charter.

In Justice Brennan's words, the values protected by "Article III are too central to our constitutional scheme to risk their incremental erosion." *Commodities Futures Trading Comm'n v. Schor*, *supra*, 478 U.S. at 861 (Brennan, J., dissenting). Permitting non-Article III bankruptcy judges to exercise final decisional authority over state law tort claims on matters of private right – matters within the core of the judicial power vested in our Article III judges – would put the Court on just that risky path.

CONCLUSION

The judgment of the Court of Appeals should be affirmed.

Respectfully submitted.

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December 2010

AMICUS CURIAE BRIEF

Supreme Court, U.S.
FILED
NOV 19 2010
OFFICE OF THE CLERK

No. 10-179

In The
Supreme Court of the United States

♦

HOWARD K. STERN, EXECUTOR OF THE ESTATE OF VICKIE LYNN MARSHALL,

Petitioner,

v.

ELAINE T. MARSHALL, EXECUTRIX OF THE ESTATE OF E. PIERCE MARSHALL,

Respondent.

♦

ON WRIT OF CERTIORARI TO
THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

♦

BRIEF OF NATIONAL ASSOCIATION OF BANKRUPTCY TRUSTEES AS AMICUS CURIAE IN SUPPORT OF PETITIONER

♦

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STATEMENT OF INTEREST OF NABT AS *AMICUS CURIAE*[1]

The National Association of Bankruptcy Trustees (NABT) is a non-profit professional association formed in 1982 to address the needs of chapter 7 bankruptcy trustees throughout the country, and to promote the effectiveness of the bankruptcy system as a whole. There are approximately 1,200 bankruptcy trustees currently receiving new cases, and approximately 900 of them are NABT members. In forty-eight states and the federal territories, the United States Trustee has the responsibility for appointing chapter 7 panel trustees pursuant to 28 U.S.C. § 586(a)(1).[2]

The United States Trustee appoints a bankruptcy trustee in every chapter 7 case. The trustee has primary responsibility for all aspects of case administration. In cases where there are assets, and a

[1] Undersigned counsel authored this brief in its entirety, and no other person or entity, other than NABT, has made any monetary contribution to the preparation or submission of this brief. Consent of all parties to the submission of *amicus curiae* briefs has been lodged with the Clerk of the Court.

[2] Pursuant to 28 U.S.C. § 581, the United States Trustee program operates in most of the nation. In North Carolina and Alabama the responsibilities of the United States Trustee program remain with the Bankruptcy Court. See Bankruptcy Judges, United States Trustees, and Family Farmer Bankruptcy Act of 1986, Pub. L. No. 99-554, 100 Stat. 3119, § 302(d)(3) (excluding North Carolina and Alabama from changes made to the Bankruptcy Code in conjunction with the expansion of the United States Trustee program elsewhere in that legislation).

prospect for distribution to creditors,[3] this includes review and objection to proofs of claim, and, if warranted, filing objections and counterclaims thereto.

This appeal addresses the issue of whether 28 U.S.C. § 157(b)(2)(C) violates Article III of the Constitution by conferring upon bankruptcy courts core jurisdiction to adjudicate compulsory counterclaims to creditors' proofs of claim filed in bankruptcy cases. The NABT supports the Petitioner's position that adjudication of compulsory counterclaims falls under the bankruptcy court's core jurisdiction and that Congress' grant of core jurisdiction to non-Article III judges is constitutional.

This Court's decision is important because it will affect the ability of trustees throughout the country to efficiently and cost-effectively administer chapter 7 cases in accordance with their fiduciary mandates under the Bankruptcy Code. The adjudication in a single forum of a creditor's proof of claim and any compulsory counterclaim to that proof of claim is vital to chapter 7 trustees' ability to effec-

[3] Generally, about 5 to 10% of chapter 7 cases are "asset" cases. In FY 2009, there were 961,025 chapter 7 cases filed; for that period there were 50,530 chapter 7 asset cases closed with $2.46 billion distributed to creditors by trustees. See United States Trustee Program Annual Report of Significant Accomplishments for Fiscal Year 2009, http://www.justice.gov/ust/eo/public_affairs/annualreport/docs/ar2009.pdf. In FY 2008, 659,568 chapter 7 cases were filed, with 69,338 asset cases closed and $3.04 billion distributed to creditors by trustees. See United States Trustee Program Annual Report of Significant Accomplishments for Fiscal Year 2008, http://www.justice.gov/ust/eo/public_affairs/annualreport/docs/ar2008.pdf.

tively and efficiently perform their duties under the Bankruptcy Code.

The duties of chapter 7 trustees are generally defined in 11 U.S.C. § 704. In addition, chapter 7 trustees follow a substantial handbook issued by the Executive Office for United States Trustees.[4] The UST Handbook governs, in varying levels of detail, a wide variety of practices and procedures pertaining to chapter 7 cases. Under § 704, as elaborated upon in the UST Handbook, trustees are duty-bound to close a bankruptcy estate as expeditiously as is compatible with the best interests of the estate.[5]

This Court's rejection of a bankruptcy judge's authority to adjudicate compulsory counterclaims would require trustees to litigate objections to creditors' claims and compulsory counterclaims asserted against them in the already busy district courts. Or, it could require that trustees undertake two separate proceedings: litigation of objections to the claims in the bankruptcy court and then a second action in the district court seeking affirmative recovery by the estate for any compulsory counterclaim to such proofs of claim.

[4] See Handbook for Chapter 7 Trustees, www.justice.gov/ust/eo/private_trustee/library/chapter07/docs/ch7_handbook/ch7_handbook_pii_2010 ("UST Handbook").

[5] See 11 U.S.C. § 704(a)(1); see also UST Handbook at pp. 6-1, 8-42. As stated in the UST Handbook: "Delays in case closure diminish returns to creditors, undermine the creditors' and public's confidence in the bankruptcy system, increase the trustee's exposure to liabilities, raise the costs of administration, and, in cases involving non-dischargeable tax liabilities, expose the debtor to increased penalties and interest. Delays also give rise to public criticism of the bankruptcy process." *Id.* at 8-42.

Moving the claims-allowance process to the district courts, or requiring two separate proceedings, rather than completing the claims-allowance process in the bankruptcy court, would place further burdens upon the courts and trustees – already challenged with additional administrative burdens under BAPCPA.[6] The end result would be diminished and delayed returns to creditors and exposure of the bankruptcy estate and debtors to increased costs. Thus, the NABT supports the position of Petitioner and files this *pro bono amicus* brief to assist the Court in recognizing the practical impact of its ruling on bankruptcy trustees and the estates they administer.

SUMMARY OF ARGUMENT

Chapter 7 trustees, as the fiduciaries responsible for the administration of all chapter 7 bankruptcy cases, are charged with preserving and promoting the system's integrity by, among other things, efficiently administering their bankruptcy cases. This includes objecting to objectionable claims and prosecuting counterclaims against parties filing claims against the estate. See 11 U.S.C.

[6] Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23. (BAPCPA). Under BAPCPA, trustees are now responsible for giving notices to child support claimants. 11 U.S.C. § 704(a)(10), (c). If the debtor had an employee benefits plan, the trustee now assumes the responsibilities of the plan administrator under the Employee Retirement Income Security Act of 1974, 29 U.S.C. § 1002. See 11 U.S.C. § 704(a)(11). In health care cases, trustees are responsible for maintaining and disposing of patient medical records, and must use all reasonable and best efforts to transfer patients to other appropriate health care facilities. See 11 U.S.C. § 704(a)(12), § 351.

§§ 704(a)(1), 704(a)(5), 502(b), 502(d), and 558; 28 U.S.C. § 157(b), (c).

Allowing bankruptcy courts to enter final judgments through a unitary claims-allowance process – with a single adjudication of creditors' proofs of claim and any compulsory counterclaims the estate has in defense of such claims – promotes administrative efficiency. Moreover, such a unitary process does not unconstitutionally vest bankruptcy judges with Article III powers. Rather, it represents an easily administrable jurisdictional scheme replete with constitutional safeguards. This jurisdictional framework,[7] in turn, supports a constitutional adjudication for creditors filing claims in bankruptcy cases – seeking payment from bankruptcy estates.

ARGUMENT

I. BANKRUPTCY TRUSTEES REQUIRE A UNITARY CLAIMS ALLOWANCE PROCESS IN ORDER TO EFFICIENTLY ADMINISTER THEIR CASES.

In order to partake in a monetary distribution from a bankruptcy estate, a creditor must file a proof of claim. 11 U.S.C. § 501. If a creditor files a proof of claim and no objection is made, then the proof of claim is deemed allowed. 11 U.S.C. § 502(a). If an objection is filed, the bankruptcy court must determine whether the claim should be allowed, and if so, in what amount. 11 U.S.C. § 502(b); 28 U.S.C. § 157(b)(2)(B) and (C).

[7] See Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 333 (1984 Act).

As with claims made in other judicial proceedings, a trustee must evaluate whether there is a compulsory counterclaim to a creditor's claim, and if so, she *must* assert it in the objection to claim proceeding. See Fed. R. Bankr. P. 7013. If a compulsory counterclaim is not asserted in the objection to claim proceeding, then, as in other judicial proceedings, the claim will be forever barred. See Charles Alan Wright et al., 6 Fed. Prac. & Proc. Civ. § 1401 (3d ed.).

As illustrated by the magnitude of asset cases that trustees administer, and corresponding claims objections they undertake in their administration of these cases, it is essential that the claims allowance/disallowance process be efficient. Congress recognized this in enacting 28 U.S.C. § 157(b)(2)(B) and (C), which confers core jurisdiction on bankruptcy courts to adjudicate all issues integral to the claims allowance/disallowance process. This includes adjudication of compulsory counterclaims against parties filing proofs of claim in bankruptcy cases. 28 U.S.C. § 157(b)(2)(C).

Indeed, the efficient administration of bankruptcy cases was a primary goal of the 1984 Act, wherein Congress sought to ensure that the core jurisdiction delineated in § 157(b) would be construed as broadly as possible in order to foster the goal of administrative efficiency. See *In re CBI Holdings Co.*, 529 F.3d 432, 459-460 (2d Cir. 2008). This legislative purpose of the 1984 Act comports with this Court's long-standing view concerning the need for efficiency in bankruptcy proceedings. See *Katchen v. Landy*, 382 U.S. 323, 328 (1966)("a chief purpose of the bankruptcy laws is to secure a prompt and effec-

tual administration and settlement of the estate"); *Bailey v. Glover*, 88 U.S. (21 Wall.) 342, 346-47 (1874); Cf. *Commodity Futures Trading Comm'n v. Schor*, 478 U.S. 833, 851, 855 (1986) (*Schor*) (admonishing "formalistic and unbending rules" that "unduly restrict Congress' ability to take needed and innovative action pursuant to its Article I powers"; holding CFTC constitutionally authorized to adjudicate compulsory counterclaims so as to promote "inexpensive and expeditious" claims resolution process).

As highlighted by the *Amici* Professors in their brief supporting Petitioner, this Court recently stressed the importance of administrative ease and efficiency in *Hertz v. Friend*, ---U.S.---, 130 S. Ct. 1181, 1193 (2010). There, this Court chided jurisdictional complexity and administrative inefficiency, saying:

> [A]dministrative simplicity is a major virtue in a jurisdictional statute. . . . Complex jurisdictional tests complicate a case, eating up time and money as the parties litigate, not the merits of their claims, but which court is the right court to decide those claims. . . . Complex tests produce appeals and reversals, encourage gamesmanship, and, again, diminish the likelihood that results and settlements will reflect a claim's legal and factual merits. Judicial resources too are at stake.

Id. at 1193.

Nonetheless, the Ninth Circuit opines that compulsory counterclaims must undergo a second-tier analysis to determine whether they are core or non-core, seemingly expunging § 157(b)(2)(C) from the bankruptcy court's jurisdictional ambit. This two-step analysis contravenes the language of § 157(b)(2)(C) and the congressional intent behind it. On the contrary, it creates a complex jurisdictional test that would eat up time and deplete estate and judicial resources. This Court has consistently reproached such overly formalistic rules that unduly restrict Congress' exercise of Article I powers to create simple jurisdictional schemes that provide due process and promote judicial efficiency. See *Schor*, 478 U.S. at 851, 855; *Thomas v. Union Carbide Agricultural Products Co.*, 473 U.S. 568, 586-589 (1985); *Crowell v. Benson*, 285 U.S. 22, 53-54 (1932). The same rationale applies here.

II. THE CLAIMS ALLOWANCE PROCESS UNDER THE PRESENT JURISDICTIONAL SCHEME IS CONSTITUTIONAL – ALLOWING BANKRUPTCY JUDGES TO FINALLY ADJUDICATE COMPULSORY COUNTERCLAIMS TO PROOFS OF CLAIM.

In this bankruptcy case, the creditor[8] filed a proof of claim and a separate adversary proceeding, to which the debtor[9] objected and filed a counter-

[8] The creditor is Pierce Marshall; his probate estate is Respondent herein.

[9] The debtor is Vickie Lynn Marshall; her probate estate is Petitioner herein.

claim.[10] The bankruptcy court ruled that the debtor's counterclaim was compulsory – arising out of the same transactions and occurrences as the creditor's proof of claim. Thereafter, and before a ruling by the state court, the bankruptcy court rendered decisions against the creditor on his adversary complaint and in favor of the debtor on her counterclaim – awarding significant damages to the debtor's bankruptcy estate.[11]

This procedural scenario follows a standard course for prosecuting compulsory counterclaims to creditors' proofs of claim, as outlined in Argument I above. The Bankruptcy Code (as amended by the 1984 Act) and this Court's jurisprudence before and after its *Marathon*[12] decision, instructs that under this scenario, the bankruptcy court constitutionally rendered the first final judgment regarding the debtor's counterclaim against the creditor's proof of claim. *In re Marshall*, 253 B.R. 550 (Bankr. C.D.Cal. 2000).

Before *Marathon*, this Court acknowledged that the equitable claims-allowance process in bankruptcy proceedings included final adjudication of

[10] See Brief of Petitioner (Pet. Br.), Statement of the Case, Bankruptcy Proceedings. Pet. Br. pp. 2-5.

[11] Respondent commenced a non-dischargeability complaint under 11 U.S.C. § 523(a)(2)(6) (willful and malicious injury) and filed a proof of claim attaching the complaint. Petitioner filed counterclaims to Respondent's proof of claim. *Id.* See also *Marshall v. Marshall*, 547 U.S. 293, 294 (2006).

[12] *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982) (*Marathon*). For discussion of *Marathon*, see Prof. Br. pp. 8-11.

compulsory counterclaims to proofs of claim. See *Katchen v. Landy*, 382 U.S. 323 (1966). After *Marathon*, this Court affirmed its rationale that by submitting proofs of claims in bankruptcy cases, creditors subject themselves to the bankruptcy court's equitable power,[13] including waiver of jury-trial rights and final adjudication of preferences and fraudulent conveyances. See *Granfianciera v. Nordberg*, 492 U.S. 33 (1989); *Langenkamp v. Culp*, 492 U.S. 42 (1990).

Thus, this Court's decisions in *Katchen*, *Granfinanciera* and *Langenkamp* fortify the constitutionality of Congress' grant of authority to bankruptcy judges to finally adjudicate compulsory counterclaims to proofs of claim.[14] Therefore – inasmuch as Petitioner's counterclaim to Respondent's proof of claim was compulsory – the bankruptcy judge was empowered to adjudicate it.

CONCLUSION

Based on the foregoing, the National Association of Bankruptcy Trustees, as *Amicus Curiae* for Petitioner, requests that the decision of the Ninth Circuit Court of Appeals be reversed.

[13] See *Young v. United States*, 535 U.S. 43, 50 (2002) citing *Pepper v. Litton*, 308 U.S. 295, 304 (1939) (recognizing that the Bankruptcy Code incorporates traditional equitable principles). For discussion of the development of the bankruptcy court's equitable jurisdiction, see Prof. Br. pp. 6, 24-27.

[14] For discussion of constitutional safeguards to non-Article III bankruptcy judges adjudicating compulsory counterclaims under the present jurisdictional system, see Prof. Br. pp. 11-17.

Respectfully submitted,

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AMICUS CURIAE BRIEF

Supreme Court, U.S.
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DEC 20 2010
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Respondent.

♦

**On Writ Of Certiorari To The
United States Court Of Appeals
For The Ninth Circuit**

♦

BRIEF FOR THE NATIONAL BLACK CHAMBER OF COMMERCE AND THE AMERICAN BOARD OF TRIAL ADVOCATES AS *AMICI CURIAE* IN SUPPORT OF RESPONDENT

♦

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QUESTIONS PRESENTED

1. Whether the Ninth Circuit opinion contravenes Congress's intent in enacting 28 U.S.C. § 157(b)(2)(C).

2. Whether Congress may, under Articles I and III, constitutionally authorize core jurisdiction over debtors' compulsory counterclaims to proofs of claim.

3. Whether allowing non-Article III bankruptcy judges to enter final judgment on all compulsory counterclaims to proofs of claim would violate personal injury plaintiffs' Seventh Amendment right to trial by jury.

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INTEREST OF *AMICI CURIAE*

The National Black Chamber of Commerce is a nonprofit, nonpartisan, nonsectarian organization dedicated to the economic empowerment of African American communities through entrepreneurship. Incorporated in 1993, it represents nearly 100,000 African American-owned businesses, and advocates on behalf of the one million Black-owned businesses in the United States. The Chamber has 190 affiliated chapters located throughout the nation, as well as international affiliates in, among others, the Bahamas, Brazil, Colombia, Ghana, and Jamaica.[1]

The Chamber is committed to furthering the rule of law and due process under law, which are key to protecting its members' rights and ensuring their economic success. To that end, the Chamber has undertaken to educate its members on a variety of matters of law, from those impacting business directly, such as government contracting, to those implicating constitutional rights and civil rights. Chamber officials write and speak regularly on legal issues that bear on the Black business community's continued growth and achievement in the face of multiple barriers to accomplishment. Chamber officials have

[1] Pursuant to Supreme Court Rule 37.6, counsel for amici represents that it entirely authored this brief and no party, its counsel, or any other entity but amici and their counsel made a monetary contribution to fund the brief's preparation or submission. All parties have consented to the filing of this brief. Letters reflecting their consent are filed with the Clerk.

also testified on these issues before Congress numerous times.

Laws that impact economic rights pose challenges to businesses, and this is particularly so of bankruptcy law, which has the potential to upset rights and obligations between private parties. Minority-owned automobile dealers, for example, were among the hardest hit by the government-managed bankruptcies of General Motors and Chrysler.[2] On the basis of its experience and that of its members, the National Black Chamber of Commerce is gravely concerned that, if bankruptcy is allowed to supplant Article III adjudication, the quality of justice will suffer.

For more than fifty years, the American Board of Trial Advocates (ABOTA), a by-invitation organization of both plaintiffs' and defendants' attorneys who have demonstrated excellence in the profession, has fought to preserve inviolate the right to trial by jury in civil cases guaranteed by the Seventh Amendment. The result sought in this matter by Petitioner would, if granted, violate that constitutionally guaranteed right. It is that threat to this valuable right, which is

[2] *Ramifications of Auto Industry Bankruptcies: Hearing Before the H Comm. On the Judiciary*, 111th Cong. 14-17 (2009) (statement of Damon Lester, National Association of Minority Automobile Dealers).

guaranteed to all civil litigants, that has prompted ABOTA to appear as amicus curiae before this Court.

♦

SUMMARY OF ARGUMENT

Article III of the United States Constitution "protect[s] the role of the independent judiciary within the constitutional scheme of tripartite government and assure impartial adjudication in federal courts." *Thomas v. Union Carbide Agric. Prods. Co.*, 473 U.S. 568, 583-84 (1985). When Congress attempts to intrude on the judicial role, the separation of powers is breached and impartial adjudication is threatened.

The vesting of power in the bankruptcy courts is, of course, a legitimate exercise of Congress's Article I power to establish "uniform Laws on the subject of Bankruptcies throughout the United States." U.S. Const. art. I, § 8, cl. 4. But the Bankruptcy Clause cannot be read so broadly so as to allow significant intrusions on the "judicial Power" expressly assigned to Article III courts. To do so would aggrandize the Legislative Branch at the expense of the Judicial. Accordingly, the Court has long recognized that Congress's power to confer jurisdiction[3] on non-Article

[3] "Jurisdiction," as used in this brief, refers to the bankruptcy court's power to issue final orders regarding a claim, absent the consent of the parties. *See* 28 U.S.C. § 157(b) A bankruptcy court may hear claims over which it lacks jurisdiction, in this sense,

(Continued on following page)

III bodies is limited. *See Commodity Futures Trading Comm'n v. Schor,* 478 U.S. 833, 850 (1986) (listing cases). Principles of federalism are also implicated when Congress assigns state-law claims to non-Article III courts.

To avoid these constitutional infirmities, 28 U.S.C. § 157(b), which defines bankruptcy judges' power to "hear and determine . . . all core proceedings" arising in a Chapter 11 bankruptcy, must be given its natural meaning as excluding the adjudication of ancillary claims inessential to resolution of the estate.

This result is no mere exercise in constitutional formalism, but a pragmatic recognition of the Framers' approach to preserving liberty and achieving justice. Bankruptcy judges lack the essential attributes of their Article III counterparts: life tenure during good behavior and compensation that may not be diminished during that tenure. Further, bankruptcy procedure – focused on the quick resolution of insolvent estates – entails a haste that may be at times incompatible with the procedural regularities that traditionally attend private lawsuits. These characteristics may further bankruptcy courts' core role of expeditiously resolving the bankruptcy estate, but they

but acts as a special master, submitting proposed findings of fact and conclusions of law to the district court, which in turn considers them *de novo*. 28 U.S.C. § 157(c)(1).

nonetheless counsel against application to claims that are ancillary to the bankruptcy estate.

Finally, the Petitioner presents arguments that would, if accepted by this Court, significantly undermine the broad personal injury exception stated in the Bankruptcy Code and impermissibly restrict the right to trial by jury in civil cases. Specifically, Petitioner asserts that bankruptcy courts have jurisdiction to resolve *any* compulsory counterclaim by the debtor, even one asserted against a personal injury claim over which the bankruptcy court wholly lacks jurisdiction, and that the "personal injury" exception to bankruptcy jurisdiction should be read narrowly to include only claims involving bodily injury. These arguments threaten to deprive injured persons of their constitutional right to trial by jury.

♦

ARGUMENT

I. Bankruptcy Court Adjudication Of Counterclaims That Are Not Necessary To Resolve The Bankruptcy Estate Is Unconstitutional

"The judicial Power of the United States, shall be vested in one supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish." U.S. Const. art. III, § 1. This command necessarily tempers Congress's authority to empower adjudicatory bodies in the exercise of its Article I powers, as those bodies may not impermissibly encroach on the Article III courts' judicial power.

For that reason, and under the Court's precedents, Congress may not assign bankruptcy courts the power to decide claims that are not necessary to resolve creditors' claims against a bankruptcy estate.

A. Congress's Power To Confer Jurisdiction On Non-Article III Courts Is Limited

The "judicial Power" that Article III vests in the courts established according to its dictates, though put in absolute terms, is broad but not plenary. "[T]he literal command of Art. III . . . must be interpreted in light of the historical context in which the Constitution was written, and of the structural imperatives of the Constitution as a whole." *Northern Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 64 (1982). There is strong basis in history and practice for adjudication of specific types of matters in venues other than the Article III courts. Courts-martial and military commissions, for example, predate the Revolution and continued in use uninterrupted through the ratification of the Constitution, with little indication that their proceedings were to be subsumed into the "judicial Power." *See generally* Detlev Vagts, *Military Commissions: A Concise History*, 101 Am. J. Int'l L. 35 (2007). Bankruptcy proceedings are likewise rooted in the Nation's history, and were employed as early as 1800. *See* "An Act to establish a Uniform System of Bankruptcy throughout the United States," 2 Stat. 19 (1800) (establishing system of bankruptcy "commissioners"). *See generally* David

Skeel, *Debt's Dominion: A History of Bankruptcy Law in America* 21-70 (2001).

The plurality opinion in *Marathon* synthesized this historical practice by identifying "three narrow situations not subject to [the Judicial Vesting Clause's] command." *Marathon*, 458 U.S. at 64. These are territorial courts, which operate where no State is a sovereign; courts-martial and related proceedings, premised on historical practice and specific assignments of power to the Executive and Congress; and legislative courts and administrative agencies created by Congress to adjudicate cases involving "public rights." *Id.* at 65-67.

It is the final category that is at issue in the present case. "Public rights" encompasses matters "that Congress would be free to commit . . . completely to nonjudicial executive determination," such that "there can be no constitutional objection to Congress' employing the less drastic expedient of committing their determination to a legislative court or an administrative agency." *Id.* at 68. Thus, this category does not threaten the separation of powers or "the Framers' vision of an independent Federal Judiciary." *Id.* at 70 n.25. It includes administrative disputes between the government and its agents, *Murray's Lessee v. Hoboken Land & Improvement Co.*, 59 (18 How.) U.S. 272 (1856), decisions that might otherwise be assigned to the discretionary authority of agency personnel, *Thomas*, 473 U.S. at 568, and narrow

categories of claims intertwined with a public regulatory scheme, *Schor*, 478 U.S. at 833.[4]

By contrast, rights and obligations between private parties involve, in nearly all instances, "private rights." Though public rights may be assigned to adjudication before non-Article III bodies, lacking "the essential attributes of the judicial power," "'[w]holly private tort, contract, and property cases, as well as a vast range of other cases, are not at all implicated'" in that allowance. *Granfinanciera v. Nordberg*, 492 U.S. 33, 53, 51 (1989) (quoting *Atlas Roofing Co. v. Occupational Safety & Health Review Comm'n*, 430 U.S. 442, 458 (1977)). In a suit between private parties, the appropriate test is whether "'a seemingly "private" right [ ] is so closely integrated into a public regulatory scheme as to be a matter appropriate for agency resolution with limited involvement by the Article III judiciary.'" *Id.* at 54 (quoting *Thomas*, 473 U.S. at 593-94). If not, the matter "must be adjudicated by an Article III court." *Id.* at 55.

[4] *See also Crowell v Benson*, 285 U.S. 22, 46 (1932) (allowing administrative adjudication of public law claims to proceed where "[t]o hold otherwise would be to defeat the obvious purpose of the legislation to furnish a prompt, continuous, expert, and inexpensive method for dealing with a class of questions of fact which are peculiarly suited to examination and determination by an administrative agency specially assigned to that task").

The Court has identified four factors relevant to the inquiry of whether a grant of power to an Article I tribunal implicates private rights:

> the extent to which the "essential attributes of judicial power" are reserved to Article III courts, and, conversely, the extent to which the non-Article III forum exercises the range of jurisdiction and powers normally vested only in Article III courts, the origins and importance of the right to be adjudicated, and the concerns that drove Congress to depart from the requirements of Article III.

Schor, 473 U.S. at 851.

Thus, in *Schor*, the Court upheld agency adjudication of a counterclaim by a commodities broker against its customers who had filed reparations complaints with the Commodity Futures Trading Commission ("CFTC"). *Id.* at 837-38, 856. First, the agency "deals only with a particularized area of law," claims related to violations of commodities trading law, and, second, "does not exercise all ordinary powers of district courts." *Id.* at 852-53 (internal quotation marks omitted). Third, "the decision to invoke this [Article I] forum is left entirely to the parties," and therefore did not limit the federal judiciary's power to take jurisdiction. *Id.* at 855. Fourth, the grant of jurisdiction to the CFTC was necessary to "mak[e] effective a specific and limited federal regulatory scheme," carried out by an expert agency in a highly technical area of the law. *Id.* at 855-56. In particular, counterclaim jurisdiction was

"necessary to make the reparations procedure workable," "incidental to, and completely dependent upon, adjudication of reparations claims created by federal law," and "limited to claims arising out of the same transaction or occurrence." *Id.* at 856. Taken together, and despite the Court's usual "searching" examination when Congress provides an alternative forum for claims traditionally held in the courts, *id.* at 854, these factors demonstrated that any encroachment on the judicial power was "de minimis." *Id.* at 856.

By contrast, a majority of the Court (across a plurality opinion and concurring opinion) in *Marathon* found that "adjudication of state-created private rights, such as the right to recover contract damages," in a bankruptcy proceeding implicated wholly private rights unsusceptible to adjudication by bankruptcy judges imbued with only Article I powers. 458 U.S. at 71. At issue in that case was the 1978 Bankruptcy Act, which assigned bankruptcy courts jurisdiction over all "civil proceedings arising under title 11 or arising in or related to cases under title 11." 28 U.S.C. § 1471(b) (1976 ed., Supp.IV). Relying on this jurisdiction, a Chapter 11 debtor filed suit in bankruptcy court against a third party for breach of contract and related claims that arose prior to its filing. 458 U.S. at 56.

Though acknowledging that the "restructuring of debtor-creditor relations" may be a "public right" subject to non-Article III adjudication, the Court held that the grant of ancillary jurisdiction to hear claims such as those at issue "carries the possibility of . . .

unwarranted encroachment" on the judicial power. *Id.* at 71, 84. It premised that conclusion on two findings. First, the bankruptcy courts had been granted authority to adjudicate rights not created by Congress, but traditional to common law and Article III adjudication. *Id.* at 81-82. Second, it assigned a broad – rather than "specialized" and "narrowly confined" – degree of subject matter jurisdiction to the bankruptcy courts, while empowering them to enter final orders not subject to *de novo* review. *Id.* at 85. In short, the statutory scheme brooked "no limiting principle" to bar efforts "to supplant completely our system of adjudication in independent Art. III tribunals and replace it with a system of 'specialized' legislative courts." *Id.* at 73.

A final limitation on Congress's power to assign adjudicatory powers to Article I tribunals is that those tribunals' determination of their jurisdiction must be subject to de novo review by an Article III court. *Crowell*, 285 U.S. at 54-55. *Crowell* concerned a workman's compensation scheme for those in maritime employment injured on the navigable waters of the United States. While upholding the assignment of adjudicatory authority to a "Compensation Commission," the Court held that the Commission could not be the final arbiter of the facts underlying whether a claim fell within its purview – that is, whether the injury occurred on the water and whether there existed a master-servant relationship. *Id.* Because "Congress cannot reach beyond the constitutional limits which are inherent in the admiralty and

maritime jurisdiction," a specialized area in which it could create such an adjudicatory scheme, the determination of jurisdiction must be subject to de novo review by an Article III court. *Id.* at 62.

B. Bankruptcy Court Adjudication Of Ancillary Disputes Over "Private Rights" Violates Fundamental Separation Of Powers Principles

There can be no question but that the controversy underlying this case implicates a "private right." The Respondent's claim – assuming *arguendo* that he had actually presented one to the bankruptcy court, *In re Marshall*, 600 F.3d 1037, 1065-66 (2010) (Kleinfeld, J., concurring) – and the Petitioner's counterclaim are private, common law torts that do not, themselves, implicate any "rights of the public." *Granfinanciera*, 492 U.S. at 68 (Scalia, J., concurring). The question, then, is whether an interpretation of 28 U.S.C. § 157(b) that provides a bankruptcy court jurisdiction to hear such a claim supplants the Article III courts' judicial power.

The adjudicatory authority Petitioner claims on behalf of the bankruptcy courts is far broader than that at issue in *Schor* in four specific ways. First, bankruptcy, by its nature, is limited to no "particularized area of the law," but reaches any possible claim by or against the debtor's estate. Though bankruptcy practice is technical and specialized, the adjudication of damages claims is the role of every trial judge. This

breadth is not, in itself, fatal – were it so, the Bankruptcy Power would be a nullity, or nearly so – but it does require a more "searching" examination of the limits on the jurisdiction and the manner in which the rights at stake are adjudicated. *Schor*, 478 U.S. at 854.

Second, in "core" proceedings, the bankruptcy court exercises all the ordinary powers of the district court, such as conducting hearings, finding facts, and entering final orders. This is so by operation of statute, and is independent from Petitioner's interpretation of the law. *See* 28 U.S.C. § 157(b)(1). Its factual determinations are not subject to plenary review by an Article III court, and there is no exception for its jurisdictional fact-finding. *See* Fed. R. Bankr. P. 8013.

Third, the decision whether to submit to the jurisdiction of the bankruptcy court is not entirely consensual, as the facts of the present case demonstrate. To preserve his claim, Respondent's predecessor was required to seek a declaration of nondischargeability from the bankruptcy court, which, in turn, subjected him to Petitioners' counterclaim; his only alternative was to abandon his claim against Petitioner in its entirety, notwithstanding its legal merits and the fact that it was pending in state court. This attribute of bankruptcy practice pulls into the estate many claims that would otherwise fall outside of the bankruptcy court's jurisdiction and that ordinarily would proceed in state or federal courts. Litigants may therefore face the same situation as the defendant in *Marathon*: being subject, without

consent, to bankruptcy jurisdiction over claims unrelated to the resolution of the bankruptcy estate.

Fourth and finally, this extended jurisdiction is not necessary to "make effective a specific and limited" regulatory scheme. To the contrary, Congress put any number of claims that may be conducive to the settlement of the state outside of the bankruptcy court's jurisdiction. 28 U.S.C. § 157(c) (non-core claims). Within its jurisdiction, however, are every possible proceeding relating to the administration of the estate, claims filed upon the estate, and the disposition of the estate's property. § 157(b)(2). Perhaps most importantly, the estate's claims are not unrecoverable if they are outside of "core" jurisdiction. The trustee or debtor-in-possession may bring suit in state or federal court to collect on them, bringing assets into the estate, for the benefit of creditors, while preserving the defendant's rights and the Article III courts' plenary power.

In these ways, Petitioner conjures a doctrine of bankruptcy jurisdiction very similar to that struck down in *Marathon*. The bankruptcy court may hear and decide any possible counterclaim against a claimant, no matter how remote from the bankruptcy. The claimant, like Respondent, has little more choice than the defendant in *Marathon* whether to submit himself to the possibility of facing unlimited jurisdiction in an Article I court. Should he decline to do so, his legitimate claim is extinguished. And once the bankruptcy court has determined the facts render a

counterclaim "core," its decision is not reviewable in full by any Article III court.

Accordingly, in its essential aspects, the Petitioner's conception of bankruptcy jurisdiction is akin to the expansive jurisdiction the Court disapproved in *Marathon*. It constitutes a usurpation of the Article III courts' powers by the legislative branch – a clear violation of the separation of powers.[5]

C. Section 157(b)(2) Readily Bears A Narrower Reading That Avoids The Need For Constitutional Adjudication

The Court need not make the "delicate undertaking" of "[d]rawing the line between permissible extensions of legislative power and impermissible incursions into judicial power." *Marathon*, 458 U.S. at 84 n.35. Instead, it should avoid this constitutional question by construing 28 U.S.C. § 157(b)(2) to allow bankruptcy courts plenary jurisdiction to decide only

[5] Petitioners' broad interpretation of bankruptcy jurisdiction also intrudes upon the powers and prerogatives of the States by extending bankruptcy jurisdiction to non-diverse state-law claims that would not otherwise typically be brought in federal court. Such actions must, at the very least, be accompanied by a "clear statement" that Congress intended to use its bankruptcy power to supersede traditional state law rules. *Cf. BFB v. Resolution Trust Co.*, 511 U.S. 531, 544 (1994) (holding that that the Bankruptcy Code was not sufficiently "clear and manifest" to "displace traditional state regulation" of foreclosure sales) (internal quotation marks omitted)

core claims "arising under" the Bankruptcy Code or "arising in" a bankruptcy case.

"[A]n Act of Congress ought not be construed to violate the Constitution if any other possible construction remains available." *N.L.R.B. v. Catholic Bishop of Chicago*, 440 U.S. 490, 500 (1979). Where one possible construction "presents a significant risk" of constitutional infirmity but a second construction does not, the courts should choose the latter. *See id.* at 510-12. This doctrine is "followed out of respect for Congress, which we assume legislates in the light of constitutional limitations," *Almendarez-Torres v. United States*, 523 U.S. 224, 238 (1998), and "reflects the prudential concern that constitutional issues not be needlessly confronted." *Edward J. DeBartolo Corp. v. Florida Gulf Coast Bldg. & Const. Trades Council*, 485 U.S. 568, 575 (1988).

Petitioner effectively concedes that its reading of Section 157(b)(2)(C) requires the Court to confront these weighty constitutional issues head-on. *See* Pet. Br. 37-65 (arguing that its interpretation does not violate Article III). The Petitioner interprets the phrase "[c]ore proceedings include . . . (C) counterclaims by the estate against persons filing claims against the estate" in that subsection to mean that all compulsory counterclaims filed in response to a

creditor's proof of claim[6] are "core" and among the claims that "[b]ankruptcy judges may hear and determine," § 157(b)(1). Pet. Br. 15, 26-28.

"Statutory construction, however, is a holistic endeavor." *United Sav. Ass'n of Texas v. Timbers of Inwood Forest Assocs., Ltd.*, 484 U.S. 365, 371 (1988). And unlike in *Schor*, where the Court found that the CFTC's "authority to adjudicate counterclaims is evident on the face of the statute," 478 U.S. at 841-42, Section 157 has a natural reading that avoids constitutional infirmity.

Specifically, Section 157(b)(2) must be read together with Section 157(b)(1), which references it. Section 1571(b)(1) limits jurisdiction to "all cases under title 11 and all core proceedings *arising under* title 11, or *arising in* a case under title 11." § 157(b)(1) (emphasis added). Section 157(b)(2), in turn, provides a non-exclusive list of core proceedings. Taken together, the plain language of these interlocking provisions requires that a claim must satisfy two criteria to be subject to decision by a bankruptcy court: (1) it must "aris[e] under" the Bankruptcy Code

[6] In this instance, there is significant doubt that the Respondent actually sought to enforce his claim in the bankruptcy proceeding, rather than preserve it against discharge. *See In re Marshall*, 600 F.3d at 1065-66 (Kleinfeld, J., concurring). If this view of the record is correct, the bankruptcy court assumed the very jurisdiction that this Court struck down in *Marathon* – determining the private rights of *non-claimants* to the estate.

or "aris[e] in" a bankruptcy case, and (2) it must be "core" under Section 157(b)(2).[7]

The terms "arising under" and "arising in" have well established meanings. "Arising under" is used in other jurisdictional contexts, including 28 U.S.C. § 1331's grant of federal question jurisdiction and 28 U.S.C. § 1334(b)'s grant of district court bankruptcy subject matter jurisdiction. This latter provision was copied from Section 1471(b) of the 1978 Bankruptcy Act, and Congress provided this guidance on it at the time:

> The phrase "arising under" has a well defined and broad meaning in the jurisdictional context. By a grant of jurisdiction over all proceedings arising under title 11, the bankruptcy courts will be able to hear any matter under which a claim is made under a provision of title 11.

H.R. Rep. No. 95-595, at 445-46 (1978). *See* 1 *Collier on Bankruptcy* § 3.01[3][c][i] (Alan N. Resnick & Henry J. Sommer eds., 16th ed.) (discussing § 1334(b) in light of § 1331).

Similarly, "arising in" has an established usage premised on Congress' drafting of Section 157 in the aftermath of *Marathon*. The leading case on this point is *In re Wood*, 825 F.2d 90 (5th Cir. 1987). *Wood*

[7] Additionally, of course, the parties may consent to the hearing and determination by the bankruptcy court of certain non-core but "related" matters. 28 U.S.C. § 157(c).

concerned a claim filed on a debtor for misappropriation of corporate assets prior to the debtor's bankruptcy filing. *Id.* at 91. The district court dismissed the case for want of bankruptcy jurisdiction, and the Fifth Circuit reversed, finding that the claim was "related to" the bankruptcy, and so within the district court's bankruptcy jurisdiction, but not a "core" proceeding. *Id.* at 92, 97. The court relied on *Marathon* for the principle that "bankruptcy judges may exercise full judicial power over only those controversies that implicate the peculiar rights and powers of bankruptcy or, in Justice Brennan's words, controversies 'at the core of the federal bankruptcy power.'" *Id.* at 96 (quoting *Marathon*, 458 U.S. at 71). *Cf. Granfinanciera*, 492 U.S. at 56 (discussing "fraudulent conveyance actions by bankruptcy trustees-suits"). As the court observed, the enumeration of "core" proceedings in Section 157(b)(2) reflects this understanding of *Marathon* by referencing "those 'administrative' matters that arise only in bankruptcy cases." *Id.* at 97.

The *Wood* court's construction of the term "arising in" is necessary to render Section 157(b)(2)(O) – a sweeping provision that provides for jurisdiction over, *inter alia*, "other proceedings affecting the liquidation of assets of the estate" – something less than a grant of plenary civil power to the bankruptcy courts. For example, without this limitation, "an action to collect a prepetition account receivable is a core proceeding," as would be any proceedings "that arise out of causes of action owed by the debtor at the time the

[bankruptcy] case is filed." 1 *Collier* § 3.02[3][d][ii]. Bankruptcy court jurisdiction over such claims would contravene *Marathon*'s holding that such a claim could not, as a constitutional matter, be within bankruptcy jurisdiction. 458 U.S. at 71 (plurality); *id.* at 90 (Rehnquist, J., concurring).

Petitioner's interpretative approach, which construes Section 157(b)(2)(C)'s allowance of counterclaims in a vacuum, runs headfirst into this problem. It would abandon the "arising under" or "arising in" limitation on the language of Section 157(b)(2)(O), transforming that provision and others into plenary grants of jurisdiction to the bankruptcy courts.

Further, Petitioner's interpretation of Section 157 renders the terms "arising under" and "arising in," mere surplusage. This contradicts the Court's dictate that "we construe statutes, where possible, so as to avoid rendering superfluous any parts thereof." *Astoria Fed. Sav. & Loan Ass'n v. Solimino*, 501 U.S. 104, 112 (1991).[8]

[8] Indeed, under Petitioner's approach and the facts of this case, the "arising in" category would blend into, or even exceed, the class of cases "related to" a bankruptcy that the statute logically considers to be broader. *See In re Marshall*, 600 F.3d at 1065 ("Vickie's counterclaim was not related to the bankruptcy, because she had already been discharged and her creditors would get none of the money she sought from Pierce in her counterclaim[ ]"). This would, in effect, render whole swaths of § 157 surplusage, e.g., §§ 157(a), (c)(1), (c)(2).

Finally, Petitioner asks the Court to abrogate two overriding presumptions of statutory construction. First is the presumption of constitutionality that applies to legislative acts. *I.N.S. v. Chadha*, 462 U.S. 919, 944 (1983). "The elementary rule is that every reasonable construction must be resorted to in order to save a statute from unconstitutionality." *Hooper v. People of State of Cal.*, 155 U.S. 648, 657 (1895). *Cf. The Federalist No. 78* (Alexander Hamilton) (federal court should strike down a statute as contrary to the constitution only "[i]f there should happen to be an irreconcilable variance between the two"). In this instance, the most reasonable construction of Section 157 – and not Petitioner's – passes muster. Second is the presumption that Congress legislates in light of the opinions of the judicial branch, particularly where Congress "was aware of them" or "they were called to its attention." *Yates v. U.S.*, 354 U.S. 298, 310 (1957). The record is clear, of course, that *Marathon* was brought to Congress's attention. *See Marathon*, 458 U.S. at 88 (affording "Congress an opportunity to reconstitute the bankruptcy courts"); 130 Cong. Rec. 7489 (1984) (statement of Rep. Peter W. Rodino Jr., Chairman of the House Committee on the Judiciary).

Where "a case can be decided on either of two grounds, one involving a constitutional question, the other a question of statutory construction or general law, the Court will decide only the latter." *Ashwander v. Tennessee Valley Auth.*, 297 U.S. 288, 347 (1936) (Brandeis, J., concurring). *Cf. Catholic Bishop*, 440 U.S. at 500-02. The Court can decide this case without

accepting Petitioner's invitation to wade into delicate constitutional questions that need not be answered here.

II. Bankruptcy Court Adjudication Of Claims Properly Heard By Article III Courts Threatens The Quality Of Justice

Article III's specific protections of judicial independence were "not created for the benefit of the judges, but for the benefit of the judged."[9] Our Constitution therefore "commands that the independence of the Judiciary be jealously guarded, and it provides clear institutional protections for that independence." *Marathon,* 458 U.S. at 60. Allowing expansive bankruptcy court adjudication of private rights claims that are ancillary to the bankruptcy estate would frustrate judicial independence. It would also move bankruptcy courts away from their core competence of efficiently resolving creditor and debtor rights, to deciding unrelated common law claims.

[9] Philip B. Kurland, *The Constitution and the Tenure of Federal Judges: Some Notes from History*, 36 U. Chi L. Rev. 665, 698 (1969), quoted in The Honorable Irving Kaufman, *Chilling Judicial Independence*, 88 Yale L. J 681, 690 (1979).

A. The Framers Devised A System To Ensure Judicial Independence "For The Benefit Of The Judged"

The Framers carefully separated the judicial from the legislative and executive branches, "to secure a steady, upright, and impartial administration of the laws." *The Federalist No. 78* (Alexander Hamilton). "There is no liberty, if the power of judging be not separated from the legislative and executive powers." *Id.* (quoting Montesquieu, *The Spirit of the Law*). *See also The Federalist No. 47* (James Madison) (same), Samuel Bryan, *The Address and Reasons of Dissent of the Minority of the Convention of Pennsylvania to their Constituents*, Dec. 18, 1787. For these and other reasons, the first section of Article III "serves to protect primarily personal, rather than structural, interests." *Schor*, 478 U.S. at 848. Where "private, common law rights are at stake," the Court's "examination of the congressional attempt to control the manner in which those rights are adjudicated has been searching." *Id.* at 854. *See also Mistretta v. United States*, 488 U.S. 361, 380-83 (1989).

There is no question but that bankruptcy judges lack the essential – and constitutionally mandated – attributes of judges exercising plenary judicial power: lifetime tenure during "good behavior" and compensation that may not be diminished during that tenure. Bankruptcy judges are instead "appointed by the court of appeals of the United States for the circuit in which [a judicial district] is located." 28 U.S.C.

§ 152(a)(1). Bankruptcy judges need not be reappointed, and may be removed by the circuit's judicial council for a variety of reasons. *See* 28 U.S.C. § 152(e).

"Periodical appointments, however regulated, or by whomsoever made, would, in some way or other, be fatal to [the courts'] necessary independence." *The Federalist No. 78* (Alexander Hamilton). Allowing bankruptcy judges plenary power to adjudicate state common law claims would, therefore, abrogate the many benefits inuring from judicial independence. Independence from political forces promotes public confidence in the judiciary. *See id.* It helps to attract well-qualified persons to the federal bench. *Marathon*, 458 U.S. at 60 n.10. It also insulates judges from pressure by their colleagues, promoting judicial individualism. *Id.* at 60 n.10. This last benefit is particularly important with regard to bankruptcy judges, who are appointed (and who often wish to be re-appointed) by Article III judges.

In any event, bankruptcy court jurisdiction over claims that are largely unrelated to the debtor's estate far exceeds this Court's limited allowance of derogations from Article III and cannot be justified by any act of Respondent or similarly-situated litigants.

In *Schor*, the Supreme Court affirmed the CFTC's adjudication of a counterclaim that was integral to the CFTC's resolution of disputes between brokers and investors where the decision to invoke the CFTC's jurisdiction was "left entirely to the

parties and the power of the federal judiciary to take jurisdiction of these matters is unaffected." *Schor*, 478 U.S. at 855-56. In contrast, the counterclaim in the instant case was necessitated by a Hobson's choice: Respondent was limited to forfeiting a claim that was already pending in state court or subjecting the claim (and any compulsory counterclaims) to parallel non-Article III adjudication. Neither Petitioner's claim nor Respondent's counterclaim had any relationship to the bankruptcy proceedings. This is simply not the case of "Congress . . . mak[ing] available a quasi-judicial mechanism through which willing parties may, at their option, elect to resolve their differences." *Id.* at 855. Rather, this case involves a mandatory non-Article III adjudication through which unwilling parties may be pulled into bankruptcy court to preserve their existing state law rights.

This Court has been, and ought to be, wary of extending plenary bankruptcy court adjudication over state law private rights claims. This is particularly true in light of the constitutional difficulties discussed above. Expedited liquidation of a bankruptcy estate is a worthy goal, but it gives no license to upend the separation of powers and the federalist structure, or to intrude upon the procedural rights of persons litigating pending private law claims.

B. Appellate Review Of Bankruptcy Court Decisions Cannot Cure Its Defects

Article III appellate review of bankruptcy court decisions does not ameliorate the constitutional difficulties stemming from the bankruptcy court's adjudication of the state law claim at issue here.

As a practical matter, appellate review of bankruptcy decisions is rare and affords little opportunity for error correction or development of the law. *See* Troy A. McKenzie, *Judicial Independence, Autonomy, and the Bankruptcy Courts*, 62 Stan. L. Rev. 747, 777 (2010).

> [A]lmost no bankruptcy litigation goes farther than the bankruptcy court, and only the rare case will make it all the way to decision in a court of appeals. Between 2000 and 2007, 11,224,562 bankruptcy petitions were filed in the federal courts. During the same period, the courts of appeals received only 7106 bankruptcy appeals – or approximately one appeal for every 1580 bankruptcy cases filed below. By comparison, 1,637,700 non-prisoner civil suits were filed in the federal district courts and 132,439 appeals in civil cases in the courts of appeals – or approximately one appeal for every twelve cases filed.

Id. at 783-84 (footnotes omitted). Furthermore, in the rare instances in which appellate review *does* occur, it is highly circumscribed. Article III courts review bankruptcy courts' factual determinations only for

clear error. *See* Fed. R. Bankr. P. 8013. Consequently, appellate review is a "poor guarantor" of "'Article III' values" in bankruptcy cases. McKenzie, at 777.

In contrast, this Court has held that more Article III judicial involvement is necessary where a statute "displace[s] a traditional cause of action and affect[s] a pre-existing relationship based on" common law. The inability of the Article III courts to review factual determinations *de novo* is particularly prejudicial because bankruptcy law and procedure are often ill-suited to the adjudication of routine claims. Orderly resolution of an estate necessarily entails expedition that may be incompatible with the procedural regularities that traditionally attend private lawsuits. Extended discovery, motions practice to tease out the nuances of a claim, and trial by jury may be unavailable.

The inadequacy of bankruptcy courts for adjudicating private rights claims that are ancillary to the bankruptcy estate itself is a matter of significant interest to civil rights plaintiffs. *Amici*'s members have been party to, and will continue to be involved in, significant civil rights litigation in both state and federal courts. The occurrence of a bankruptcy event should not force civil rights plaintiffs to defend against counterclaims outside the Article III or state courts. The Ninth Circuit's decision, by separating the wheat (claims that are "part and parcel" of the claims allowance process) from the chaff (claims that are not "part and parcel" of the claims allowance process), strikes a common-sense and functional

distinction that will allow for a fast and efficient resolution of the bankruptcy process, while at the same time protecting the third parties' rights.

III. Granting The Relief Petitioner Seeks Would Violate Personal Injury Plaintiffs' Seventh Amendment Right To Trial By Jury

The Seventh Amendment provides, in pertinent part, that "where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved, and no fact tried by a jury, shall be otherwise reexamined in any Court of the United States. . . ." U.S. Const. amend. VII.

Due to Seventh Amendment concerns, the 1984 Amendment to the U.S. Bankruptcy Code specifically exempted personal injury and wrongful death claims from core proceedings that bankruptcy courts could finally adjudicate. 28 U.S.C. § 157(b)(2)(B), (O). As a result, the law provides such claims must be tried in federal district court, if they are raised in a bankruptcy proceeding. 28 U.S.C. § 157(b)(5).

Petitioner, however, asserts that bankruptcy courts have jurisdiction to resolve *any* compulsory counterclaim by the debtor, even one asserted against a personal injury claim over which the bankruptcy court would otherwise lack jurisdiction. Further, Petitioner also urges that "personal injury" in Section 157(b)(2)(B) of the Code should be read narrowly to include only claims involving bodily injury. These

arguments are contrary to the plain meaning of the statutory text, this Court's decision in *Marathon*, and the principles embodied in the Seventh Amendment.[10]

A. Petitioners' Proposed Exception To The Personal Injury Claim Exclusion Is Not Supported By The Bankruptcy Code's Plain Language.

As noted above, 28 U.S.C. § 157(b)(2) specifically exempts personal injury claims from the definition of core proceedings that may be finally adjudicated by bankruptcy courts:

> (2) Core proceedings include, but are not limited to – . . .
>
> > (B) allowance or disallowance of claims against the estate . . . *but not the liquidation or estimation of contingent or unliquidated personal injury tort or wrongful death claims against the estate* for purposes of distribution in a case under title 11.
> >
> > . . .
> >
> > (O) other proceedings affecting the liquidation of the assets of the estate or the adjustment of the debtor-creditor or the equity security holder relationship, *except*

[10] Consistent with its mission of preserving the right to trial by jury in civil cases, ABOTA's primary focus is on Part III of this Brief.

> *personal injury tort or wrongful death claims.*

28 U.S.C. § 157(b)(2) (emphasis added). In addition, Congress has specifically provided that personal injury claims may be tried *only* in district court:

> *The district court shall order that personal injury tort and wrongful death claims shall be tried in the district court* in which the bankruptcy case is pending, or in the district court in the district in which the claim arose. . . .

28 U.S.C. § 157(b)(5) (emphasis added).

The purpose of these provisions is to protect plaintiffs' rights by preventing bankruptcy courts from trying personal injury tort actions. *In re Poole Funeral Chapel, Inc.*, 63 B.R. 527, 532 (Bankr. N.D. Ala. 1986). And, as the Seventh Circuit has explained, if a bankruptcy court lacks jurisdiction over a claim under Section 157(b)(5), then "[t]he whole case, including defenses of all kinds, goes off to the district judge or the state court." *Pettibone Corp. v. Easley*, 935 F.2d 120, 123 (7th Cir. 1991).

Congress not only excepted personal injury claims from core bankruptcy court jurisdiction and dictated that such claims be tried in district court, but also specifically preserved to such claimants their right to trial by jury. Section 1411 preserves "any right to trial by jury that an individual has under applicable nonbankruptcy law with regard to a personal injury or wrongful death tort claim." 28 U.S.C.

§ 1411(a) (1998 & Supp. V 1993). Read together, these provisions not only ensure that personal injury claims are tried by an Article III judge, but that the claimant's right to trial by jury is protected as well. A personal injury claimant does not lose this right simply because he files a Proof of Claim. *See Germain v. Connecticut Nat'l Bank*, 988 F.2d 1323, 1327 (2nd Cir. 1993) (the presence of Section 157(b)(5)'s requirement that a personal injury claim be tried in district court "strongly suggests that these litigants are entitled to a jury trial in such an action even after a proof of claim has been filed in bankruptcy court").

Because of these clear provisions of the Code, bankruptcy courts lack jurisdiction over personal injury claims. *In re Arnold*, 407 B.R. 849, 851 (Bankr. M.D. N.C. 2009). Additionally, a personal injury claimant cannot consent to bankruptcy court jurisdiction by filing a proof of claim. *In re Gary Brew Enters. Ltd. v. Adams*, 198 B.R. 616, 620 (Bankr. S.D. Cal. 1996).

Notwithstanding these clear statutory restrictions, Petitioner argues that a debtor's compulsory counterclaim, resolution of which disposes of a claimant's personal injury claim, may be resolved by the bankruptcy court. That approach would deny personal injury claimants the very constitutional protections from bankruptcy court jurisdiction that Congress preserved in the Code and would deprive personal injury claimants of the right to trial by jury guaranteed by the Seventh Amendment.

The procedural history and facts are recited at length in the parties' briefs, but a brief overview is illustrative of the flaws in Petitioner's argument. In 1995, Vickie Lynn Marshall commenced probate proceedings in a Texas probate court concerning the estate of her deceased husband J. Howard Marshall, II ("J. Howard"), the father of E. Pierce Marshall ("Pierce"). She sought a declaration concerning the validity of J. Howard's estate plan, and alleged that Pierce had tortiously interfered with her property rights concerning J. Howard's assets. During those proceedings, Vickie's lawyers defamed Pierce, who filed suit in another Texas court against Vickie and her attorneys. Vickie subsequently filed for bankruptcy in California, and Pierce was compelled to dismiss her from his defamation suit. He filed a non-dischargeability complaint and proof of claim in the bankruptcy court concerning his defamation claim against Vickie.

Defamation is a personal injury claim under both federal and Texas law. *See In re Arnold*, 407 B.R. at 853; *In re Smith*, 389 B.R. 902, 908 (Bankr. D. Nev. 2008); *Newsom v. Brod,* 89 S.W.3d 732, 735 (Tex. App.-Houston [1st Dist.] 2002, no writ). Vickie filed a counterclaim asserting that Pierce interfered with an *inter vivos* gift that J. Howard intended to give her by facilitating illegitimate estate planning transactions for J. Howard. She argued that her counterclaim negated an element – falsity – of Pierce's defamation claim.

Petitioner argues that her counterclaim to Pierce's personal injury claim was a "core proceeding" under the Code because Section 157(b)(2)(C) mentions "counterclaims by the estate against persons filing claims against the estate." Thus, she suggests that this includes *any* counterclaim, including one asserted in response to a personal injury claim over which the bankruptcy court has no jurisdiction. If this position is accepted by this Court, the personal injury claim exception to bankruptcy court jurisdiction will be rendered meaningless, and the right to trial by jury guaranteed in the Seventh Amendment will have been ignored. Indeed, Petitioner's interpretation of Section 157(b)(2)(C) would vitiate a personal injury claimant's right to trial by jury in federal district court under Sections 157(2)(B), (O), and (5).

For example, because the personal injury claim *must* be tried in federal district court, Petitioner's interpretation would mean that the prosecution of the claim and defenses to it and prosecution of the counterclaim would be split between two courts, because – unlike the "counterclaim" provision – there is no provision that speaks to "defenses." Trying the counterclaim in a court different from the one in which the claim is prosecuted may lead to inconsistent results on the same facts. It is simply illogical to construe the Code to mean that Congress intended to allow a debtor to prosecute in bankruptcy court a counterclaim to a claim against the debtor that must also be brought in a district court. The interpretation urged by Petitioner violates the common mandate of

statutory construction: avoid an absurd result. *See, e.g., U.S. v. Katz,* 271 U.S. 354, 357 (1926) ("All laws are to be given a sensible construction.").

Further, if resolution of the counterclaim would defeat plaintiff's personal injury claim, its prosecution in bankruptcy court would permit, indirectly, that which Congress has clearly and directly disallowed. In the Code, Congress expressly exempted personal injury claims from bankruptcy court jurisdiction and mandated that the merits of such claims be decided in a federal district court. If the bankruptcy court is permitted, as urged by Petitioner, to decide a counterclaim that defeats an element of plaintiff's (here, Respondent's) personal injury claim, the plaintiff is denied its right to a jury trial on that claim in a district court. There is no justification for the position Petitioner would have this Court adopt, and the Seventh Amendment militates against it.

B. Allowing A Bankruptcy Court To Finally Adjudicate A Counterclaim To A Personal Injury Claim Runs Afoul Of *Marathon*

In *Marathon,* this Court held that a non-Article III bankruptcy court could not constitutionally exercise jurisdiction over a state law claim brought by the debtor against a non-consenting third party. Petitioner argues that *Marathon* is not implicated by a bankruptcy court's resolution of a state law counterclaim because the counterclaim defendant (i.e., plaintiff)

voluntarily submitted to bankruptcy court jurisdiction by filing a Proof of Claim.

A personal injury plaintiff does no such thing. By the express terms of the Code, a personal injury plaintiff who files a Proof of Claim *does not and cannot* submit to bankruptcy court jurisdiction and filing of the Proof of Claim does not make it a core proceeding. *See, e.g., In re Castlerock,* 781 F.2d 159, 163 (9th Cir. 1986) (creditor did not consent to bankruptcy court jurisdiction when, in response to counterclaim filed by debtor against creditor's Non-dischargeability Complaint, creditor filed defensive Proof of Claim); *Mohawk Indus., Inc. v. Robinson Indus., Inc.,* 46 B.R. 464, 465 (D.C. Mass. 1985) (defendant did not consent to bankruptcy court jurisdiction over debtor's claim by asserting affirmative defense). Unlike Petitioner's interpretation, limiting "counterclaims" to those in response to claims that are, themselves, within bankruptcy court subject matter jurisdiction properly avoids construing the statute in an unconstitutional manner. *Johnson v. Robison,* 415 U.S. 361, 366-67 (1974). The preferred interpretation of the Code – to the extent it requires interpretation – is one that does not deprive civil litigants of their right to trial by jury.

C. The Bankruptcy Code Language Does Not Support Interpreting "Personal Injury Claim" To Mean Only A Claim Arising From Bodily Injury

Petitioner also argues that a claim is not a personal injury claim unless it involves bodily injury. Congress, however, knew how to use the phrase "bodily injury" when that was intended. In Section 522(d)(11) of the Code, for example, Congress specifically used the phrase "personal *bodily* injury." (emphasis added). In addition, the majority of courts to address the issue have rejected this narrow reading of the term. *Compare Massey Energy Co. v. West Virginia Consumers for Justice,* 351 B.R. 348, 351 (E.D. Va. 2006) (adopting narrow, "bodily injury" only view); *Perino v. Cohen (In re Cohen),* 107 B.R. 453, 455 (S.D.N.Y. 1989) (same); *In re Atron Inc. of Michigan,* 172 B.R. 541, 545 (Bankr. W.D. Mich. 1994) (same); *Bertholet v. Harman,* 126 B.R. 413, 416 (Bankr. D.N.H. 1991) (same), *with Hansen v. Borough of Seaside Park (In re Hansen),* 164 B.R. 482, 485-86 (D.N.J. 1994) (adopting expansive view that personal injury includes broad category of private or civil wrongs or injuries); *In re Erickson,* 330 B.R. 346, 349 (Bankr. D. Conn. 2005) (same); *Rizzo v. Passialis (In re Passialis),* 292 B.R. 346, 352 (Bankr. N.D. Ill. 2003) (same); *Boyer v. Balanoff (In re Boyer),* 93 B.R. 313, 317 (Bankr. N.D.N.Y. 1988) (same); *Leathem v. Von Volkmar (In re Von Volkmar),* 218 B.R. 890, 894 (Bankr. N.D. Ill. 1998) (same); *In re Ice Cream Liquidation, Inc.,* 281 B.R. 154, 161 (Bankr. D. Conn. 2002)

(rejecting "bodily injury" view, but adopting middle ground that inquires whether claim has earmarks of financial, business or property tort claim); *Adelson v. Smith (In re Smith),* 389 B.R. 902, 908 (Bankr. D. Nev. 2008) (same).

Moreover, commercial practice recognizes that "personal injury" is much broader than "bodily injury." For example, the "personal injury" endorsement to a Commercial General Liability (CGL) insurance policy does not cover "bodily injury" at all. Rather, it covers such things as defamation, false arrest, malicious prosecution, trademark infringement, business piracy and other things much more akin to claims for civil rights violations and defamation than to a broken leg. *See, e.g., Delta Pride Catfish, Inc. v. Home Ins. Co.*, 697 So. 2d 400, 403 (Miss. 1997) (quoting personal injury endorsement policy language).

Petitioner's urged interpretation also ignores the fact that the "personal injury" exception embodies Congress's recognition that personal injury claimants stand in a different relationship with the bankruptcy debtor, because they did not voluntarily enter into dealings with the debtor, unlike a business creditor. *Adams v. Cumberland Farms, Inc.*, No. 95-1736, 1996 WL 228567, *3 (1st Cir. May 7, 1996). This principle is equally true whether the debtor has negligently injured the creditor or intentionally defamed him. If this Court were to accept Petitioner's argument, the personal injury exception will be significantly and unreasonably narrowed to only those plaintiffs who have suffered bodily harm. Other traditional "personal

injury" plaintiffs, including those whose civil rights have been violated, will lose their constitutional right to trial by jury. As a result, a substantial number of traditional personal injury plaintiffs will likely be required to prosecute their claims in bankruptcy courts that are ill-equipped to manage such trials and operate under equitable rules that differ markedly from the standardized rules of procedure and evidence followed by federal district courts and state courts.

Preservation of the Seventh Amendment right to trial by jury in civil cases demands rejection of the unwarranted construction sought by Petitioner.

•

CONCLUSION

The judgment of the Ninth Circuit should be affirmed.

Respectfully submitted,

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DECEMBER 20, 2010

AMICUS CURIAE BRIEF

Supreme Court, U.S.
FILED
DEC 20 2010
OFFICE OF THE CLERK

No. 10-179

IN THE

Supreme Court of the United States

HOWARD K. STERN, Executor
of the Estate of Vickie Lynn Marshall,
Petitioner,

v.

ELAINE T. MARSHALL, Executrix
of the Estate of E. Pierce Marshall,
Respondent.

On Writ of Certiorari
to the U.S. Court of Appeals
for the Ninth Circuit

BRIEF OF WASHINGTON LEGAL FOUNDATION AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENT

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QUESTION PRESENTED

A Texas probate court upheld the validity of an estate plan and estate planning documents prepared by J. Howard Marshall, finding that he knowingly effected his estate plan free from coercion from his son Pierce Marshall. The U.S. Court of Appeals for the Ninth Circuit concluded that the findings of the Texas probate court should be afforded preclusive effect in on-going bankruptcy proceedings involving Vickie Lynn Marshall, who was married to J. Howard Marshall in the year prior to his death in 1995. Based on that conclusion, it directed that judgment be entered in favor of the Estate of Pierce Marshall on a claim against him for tortious interference with an intervivos gift. The Estate of Vickie Lynn Marshall sought review of the appeals court's decision. The Court granted review to consider the following question:

Whether, consistent with 28 U.S.C. § 157 and Article III, a bankruptcy judge may enter final judgment on a bankruptcy estate's counterclaim against an individual who has filed a claim against the estate, where: (1) the bankruptcy court lacked jurisdiction to try the individual's claim because it was a personal injury claim; (2) resolution of the counterclaim was not a necessary precursor to resolution of the individual's claim; and (3) neither the individual's claim nor the counterclaim involved "public rights" but rather raised issues of Texas law?

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INTERESTS OF *AMICUS CURIAE*

The Washington Legal Foundation (WLF) is a public interest law and policy center with supporters in all 50 States.[1] WLF defends and promotes free enterprise, individual rights, and a limited and accountable government. WLF has appeared in this Court on numerous occasions to support its view that federal law, as well as principles of federalism, require federal courts to give full faith and credit to the judgments of state courts. *See, e.g. San Remo Hotel, L.P. v. City of San Francisco*, 545 U.S. 323 (2005); *Matsushita Electric Industrial Co. v. Epstein*, 516 U.S. 367 (1996).

For multiple reasons, WLF agrees with the appeals court's conclusion that the findings of the Texas probate court should be afforded preclusive effect in these on-going federal bankruptcy proceedings. The bankruptcy court's efforts to conduct a trial and enter a final judgment on Petitioner's tort claims far exceeded the bounds of both Article III of the Constitution and federal law. WLF is concerned that if those efforts are affirmed, the strict limitations that Congress sought to place on bankruptcy court jurisdiction will have been abandoned.

WLF agrees with the appeals court's preclusion determination for the additional reason that the Texas probate court judgment, as the last unappealed

[1] Pursuant to Supreme Court Rule 37.6, WLF states that no counsel for a party authored this brief in whole or in part; and that no person or entity, other than WLF and its counsel, made a monetary contribution intended to fund the preparation and submission of this brief. All parties have consented to the filing of this brief; letters of consent have been lodged with the clerk.

judgment entered in this case, is entitled to preclusive effect. The issues that Petitioner continues to press in these proceedings were decided conclusively against it in the Texas probate court judgment. Petitioner chose not to appeal from that judgment, nor has it sought review from the Ninth Circuit's holding that the Texas judgment conclusively decided the issues that Petitioner still seeks to press. Under those circumstances, the last-in-time rule – a rule that Respondent has asserted throughout this litigation – requires affirmance of the Ninth Circuit's preclusion determination. WLF does not believe that Petitioner's forum shopping ought to be rewarded.

STATEMENT OF THE CASE

This feud over the assets of the estate of J. Howard Marshall II has spawned three court judgments.[2] A principal issue before the Ninth Circuit was whether any of those judgments should have preclusive effect in these proceedings.

The first judgment was issued by the U.S. Bankruptcy Court for the Central District of California on December 29, 2000. The bankruptcy court determined that Pierce tortiously interfered with Vickie's expectation of an *inter vivos* gift and awarded her $450 million in compensatory damages (less any

[2] Because four of the individuals involved in this dispute – J. Howard Marshall II, Vickie Lynn Marshall, E. Pierce Marshall, and Elaine T. Marshall – share the same last name, each will be referred to herein by his or her first name only. Of those four, Elaine T. (the widow of E. Peirce and the executrix of his estate) is the only one still living.

amount recovered by Vickie in the Texas Probate Court action) and $25 million in punitive damages. *See In re Vickie Lynn Marshall* ("*Marshall I*"), 253 B.R. 550 (Bankr. C.D. Cal 2000). The district court vacated that judgment on May 24, 2001; it determined that Vickie's tortious interference claim was not a "core" bankruptcy proceeding and thus that the bankruptcy court was not empowered to enter a final judgment with respect to that claim. *In re Vickie Lynn Marshall* ("*Marshall II*"), 274 B.R. 609, 633 (C.D. Cal. 2001) (as amended on June 20, 2001). Vickie's appeal from the district court's decision to vacate the judgment was rejected by the court below. *Marshall v. Stern* ("*Marshall V*"), 600 F.3d 1037 (9th Cir. 2010).

The second final judgment was issued by the Texas Probate Court on December 7, 2001. That judgment upheld J. Howard's will and his 1982 living trust as genuine, valid, and not the product of improper conduct. Ninth Circuit Excerpts of Record ("ER") 4706. The probate court also determined that it had jurisdiction over Vickie's tortious interference claim; it rejected that claim on the merits, finding that J. Howard had not intended to make a gift to Vickie from either his estate or the living trust, and thus that Pierce was entitled to his inheritance free and clear of any claim by Vickie. ER 4721, 4718. Importantly, although Vickie actively participated in the Texas probate proceedings, she never formally asserted in those proceedings that the bankruptcy court judgment should be given preclusive effect. Under Texas law (as interpreted by the district court), a judgment becomes final for preclusion purposes when, after entry of the judgment, the 30-day period for filing a motion to amend the

judgment has expired (or the period for ruling on any such motion has expired). *Scurlock Oil Co. v. Smithwick*, 724 S.W.2d 1, 6 (Tex. 1986). This Court stated that the Probate Court judgment became final for preclusion purposes on February 11, 2002. *Marshall v. Marshall*, 547 U.S. 293, 314 (2006). Vickie did not appeal from that judgment.

The third final judgment was issued by the U.S. District Court for the Central District of California on March 7, 2002. The district court concluded that Pierce tortiously interfered with Vickie's expectancy and awarded her compensatory and punitive damages totaling $89 million. *In re Vickie Lynn Marshall* ("*Marshall IV*"), 275 B.R. 5 (C.D. Cal. 2002). The district court had previously (on December 21, 2001) rejected Pierce's request that the December 7, 2001 probate court findings be given preclusive effect. *In re Vickie Lynn Marshall* ("*Marshall III*"), 271 B.R. 858 (C.D. Cal. 2001). As part of its *Marshall V* decision (Pet. App. 1-89), the Ninth Circuit concluded that the district court erred in failing to give preclusive effect to the probate court findings. In particular, the Ninth Circuit rejected Vickie's contention that the issues she was seeking to litigate in the bankruptcy proceedings were distinct from the issues decided in the probate court. *Marshall V*, 600 F.3d at 1062-64. It also determined that Vickie had "fully and fairly litigated" those issues in the probate court. *Id.* at 1063.

Before the Ninth Circuit, Respondent raised two principal arguments regarding why preclusive effect should be given to the probate court's December 7, 2001 judgment rather than to the December 20, 2000

bankruptcy court judgment. First, Respondent argued that the bankruptcy lacked jurisdiction to enter a final judgment on Vickie's state-law counterclaim under 28 U.S.C. §157(b), but rather was authorized (at most) to submit proposed findings of fact and conclusions of law to the district court under § 157(c). Second, Respondent argued that even if the bankruptcy court was acting within its jurisdiction, the last-in-time rule required that preclusive effect be given to the later judgment – in this case, the December 7, 2001 probate court judgment.

The Ninth Circuit ruled in Respondent's favor on the first argument and thus did not need to reach the second argument. The court's ruling focused on 28 U.S.C. § 157(b), the provision that grants bankruptcy courts jurisdiction to enter final judgments in certain cases. The court held that determining whether a proceeding falls within a bankruptcy court's § 157(b) jurisdiction is a "two-step" process. First, one determines whether a proceeding is a "core proceeding" within the meaning of § 157(b)(2). If so, a bankruptcy court may enter a final judgment if the "core proceeding" "aris[es] under title 11" or "aris[es] in a case under title 11." *Marshall V*, 600 F.3d at 1055.

Petitioner contended that Vickie's tortious interference counterclaim was a "core proceeding" under § 157(b)(2)(C) (which provides that core proceedings include, but are not limited to, "counterclaims by the estate against persons filing claims against the estate"). The Ninth Circuit held that regardless whether Vickie's claim was a "core proceeding," it was not a core proceeding "in a case arising under the Bankruptcy Code" because it was "not

so closely related to Pierce Marshall's defamation claim that it must be resolved in order to determine the allowance or disallowance of his claim against her bankruptcy estate." *Id.* at 1059. The court concluded that its "closely related" standard was the proper reading of § 157(b) based on: (1) its review of the evolution of the Bankruptcy Code; (2) this Court's opinions in cases construing Article III and Seventh Amendment limitations on bankruptcy court jurisdiction; and (3) Ninth Circuit jurisprudence "cautioning against creating constitutional problems through an overly broad construction" of bankruptcy court jurisdiction. *Id.* at 1058.

The Court granted review to Petitioner on the issue of whether the Ninth Circuit properly interpreted § 157(b). Petitioner did not seek review of the Ninth Circuit's holding that the issues Vickie sought to litigate in the bankruptcy proceedings were *not* distinct from the issues decided in the probate court; thus, that holding is now final.

SUMMARY OF ARGUMENT

WLF agrees with Respondent that the bankruptcy court exceeded its jurisdiction when in December 2000 it enter a judgment on Vickie's tortious interference counterclaim. But under well-established rules governing *res judicata* and collateral estoppel, the probate court judgment would be entitled to preclusive effect even if this Court reverses the district court on this issue and determines that the bankruptcy court judgment was properly entered. When (as would be true here if the bankruptcy court judgment were deemed

properly entered) conflicting judgments have been entered by two courts, the last-in-time rule requires that preclusive effect be given to the later judgment – in this case, the probate court judgment.

WLF also agrees with Respondent that the bankruptcy court, by entering a final judgment on Vickie's state-law counterclaim, exceeded the jurisdiction granted it by 28 U.S.C. § 157(b). If the Court nonetheless interprets the statute in the manner suggested by Petitioner, then it should not hesitate to rule that § 157(b) is unconstitutional as applied in this case. The Court's Article III precedent makes clear that Congress is not permitted to authorize the federal adjudication of claims of this nature by a body other than an Article III court. Nor do the facts support a finding that Respondent has waived his Article III rights by consenting to the bankruptcy court's jurisdiction.

In adopting § 157(b), Congress did not intend to authorize a bankruptcy court to a enter final judgment on a bankruptcy estate's counterclaim of the sort at issue in this case. At the very least, Respondent has demonstrated that its interpretation of § 157(b) is highly plausible and should be adopted in order to avoid the serious constitutional difficulties that would arise if Petitioner's interpretation of § 157(b) were adopted. Were the Court to adopt the interpretation of § 157(b) espoused by Petitioner and the United States, all effective limits on the jurisdiction of bankruptcy courts would be eliminated. In responding to *Northern Pipeline*, Congress made clear that it intended to impose strict limits on that jurisdiction.

ARGUMENT

I. REGARDLESS WHETHER THE BANKRUPTCY COURT WAS EMPOWERED TO ENTER A JUDGMENT, THE PROBATE COURT JUDGMENT MUST PREVAIL UNDER THE LAST-IN-TIME RULE

J. Howard Marshall II died more than 15 years ago. Litigation over the disposition of his assets has been going on for nearly as long, and it has outlived Vickie and Pierce, the two principal adversaries. It needs to end.

WLF agrees with Respondent that the bankruptcy court exceeded its jurisdiction when in December 2000 it enter a judgment on Vickie's tortious interference counterclaim. But under well-established rules governing *res judicata* and collateral estoppel, the probate court judgment would be entitled to preclusive effect even if this Court reverses the district court on this issue and determines that the bankruptcy court judgment was properly entered. When (as would be true here if the bankruptcy court judgment were deemed properly entered) conflicting judgments have been entered by two courts, the last-in-time rule requires that preclusive effect be given to the later judgment – in this case, the probate court judgment. *See, e.g.*, RESTATEMENT (SECOND) OF JUDGMENTS, § 15 (1982).

Respondent raised the last-in-time rule in both the district court and the Ninth Circuit. The appeals court did not need to reach the issue because it held that the bankruptcy court lacked jurisdiction to enter its

judgment. But "[w]ithout cross-petitioning for certiorari, a prevailing party may, of course, defend its judgment on any ground properly raised below whether or not that ground was relied upon, rejected, or even considered by the District Court or the Court of Appeals." *14 Penn Plaza LLC v. Pyett*, 129 S. Ct. 1456, 1474 (2009) (quoting *Grandfinanciera, S.A. v. Nordberg*, 492 U.S. 33, 38-39 (1989). In her brief filed in this Court, Respondent has explicitly preserved her assertion that the last-in-time rule bars Vickie's tortious interference claim. Resp. Br. 34.

The Court, in an exercise of its discretion, often declines to address an issue that has not yet been decided by the lower courts, and if necessary will remand a case to give the court of appeals the initial opportunity to consider the issue. WLF respectfully suggests that any such remand would be inappropriate under the facts of this case. This litigation is before the Court for a second occasion. The interests of justice will not be served by allowing the case to stretch into a third decade. The basic facts regarding the course of the litigation are largely undisputed. The applicability of the last-in-time rule is clear-cut. Should the Court decide that the bankruptcy court had jurisdiction to enter a judgment on Vickie's tortious interference claim, the Court should go on to determine whether the last-in-time rule operates to bar consideration of that claim.

The last-in-time rule, which provides that the most recent of two inconsistent judgments controls, faithfully applies the principles of the Full Faith and Credit Clause and its implementing Act. The Court applied the last-in-time rule to give conclusive effect to

a later-entered judgment in *Treinies v. Sunshine Mining Co.*, 308 U.S. 66, 74-78 (1939). State courts in Washington and Idaho had issued conflicting judgments regarding ownership of stock in Sunshine Mining Co. Sunshine later filed an interpleader action, seeking guidance from the federal courts regarding ownership. The Court determined that the Idaho judgment should prevail because: (1) it was issued later; and (2) the Idaho courts (before whom all parties appeared) determined that the Washington courts lacked jurisdiction over the stock and thus that the Washington judgment was not binding; (3) the party that had prevailed in the Washington lawsuit failed to appeal from the adverse Idaho decision; and (4) issue preclusion prevented the federal courts from relitigating the jurisdictional question. *Id.* *See generally* Ruth B. Ginsburg, *Judgments in Search of Full Faith and Credit: The Last-in-Time Rule for Conflicting Judgments*, 82 HARV. L. REV. 798 (1969).

The probate court can hardly be blamed for having failed to give preclusive effect to the bankruptcy judgment. By the time the probate court issued its final judgment in December 2001, the bankruptcy court judgment had long since been vacated by the district court – so there was no existing judgment to which the probate court could have deferred. But if Vickie believed that the probate court erred in failing to defer to the bankruptcy court judgment and findings, her appropriate response would have been to appeal the judgment – all the way to the U.S. Supreme Court if necessary. Instead of pursuing such an appeal, Vickie chose to pursue a collateral attack on the probate court judgment in the federal courts. The last-in-time rule

was adopted to prevent just such collateral attacks.

Moreover, Vickie never filed any papers in the probate court asserting that the bankruptcy court judgment should be given preclusive effect. She argued in the lower federal courts that she had adequately preserved the point because one of her attorneys raised the point orally on one occasion in the probate court. But even so, any such oral assertion was inadequate to: (1) excuse her failure to take a direct appeal from the probate court judgment; or (2) explain how the probate court could be deemed to have erred given that the bankruptcy court judgment had been vacated months before the probate court issued its judgment.

This case raises a wrinkle on the last-in-time rule because the first judgment (the December 2000 bankruptcy court judgment) is still on direct appeal. Commentators are nonetheless unanimous in concluding that the last-in-time rule requires an appellate court hearing a direct appeal of the first judgment to defer to the last judgment. One leading treatise concludes:

> [O]ne of the two judgments must control, and there is no reason to depart from the general preference for the second judgment if the parties have failed to assert preclusion from the first judgment or if the second court has properly rejected the preclusion argument. The court reviewing the first judgment may be tempted to review the preclusion effects of the first judgment if there was no effective opportunity to raise the question in the second action or if rejection of the

> preclusion argument seems dubious. *That temptation should be resisted.* Unless appeals from both judgments can be consolidated before a single court, the second judgment should be reviewed only within its own system. Any claim that the court reviewing the first judgment has power to enter its own subsequent judgment that should prevail over the second judgment would simply lead to a parallel assertion that review of the second judgment can lead to yet another and most final judgment.

18 C. Wright, A. Miller, & E. Cooper, *Federal Practice and Procedure: Jurisdiction*, § 4404 at 30-31 (1981) (emphasis added).

The judgment of the probate court is final, and has been for nearly a decade. Having failed to appeal that judgment, Petitioner is not entitled at this late date to ask the Court to re-examine it. The Ninth Circuit ruled that the probate court judgment conclusively determined the issues that Vickie was seeking to press in the bankruptcy proceedings, rejecting her contention that those issues were distinct from the issues decided in the probate court. *Marshall V*, 600 F.3d at 1062-64. Accordingly, the last-in-time rule provides an alternative basis for affirming the Ninth Circuit's judgment.

II. ARTICLE III BARS BANKRUPTCY JUDGES FROM ENTERING A FINAL JUDGMENT ON A BANKRUPTCY ESTATE'S COUNTERCLAIM UNDER THE FACTS OF THIS CASE

WLF agrees with Respondent that the bankruptcy court, by entering a final judgment on Vickie's state-law counterclaim, exceeded the jurisdiction granted it by 28 U.S.C. § 157(b). If the Court nonetheless interprets the statute in the manner suggested by Petitioner, then it should not hesitate to rule that § 157(b) is unconstitutional as applied in this case. The Court's Article III precedent makes clear that Congress is not permitted to authorize the federal adjudication of claims of this nature by a body other than an Article III court.

It is common ground that, in general, the judicial power of the United States must be exercised by courts having the attributes prescribed by Article III. The Constitution explicitly sets forth those attributes:

> The Judges, both of the supreme and inferior Courts, shall hold their Offices during good Behaviour, and shall, at Stated Times, receive for their Services, a Compensation, which shall not be diminished during their Continuance in Office.

Art. III, § 1. Bankruptcy judges do not and never have possessed those attributes – they are appointed for a fixed term, they can be removed from office by means other than a congressional impeachment and trial, and their salaries are not protected from diminution by

Congress. Accordingly, all agree that bankruptcy courts do not qualify as Article III courts.

In *Northern Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982), the Court imposed strict constitutional limits on the authority of non-Article III bankruptcy courts to exercise jurisdiction over state-law claims filed by a debtor-in-possession against a third party. Although the six-justice majority could not agree on the precise rationale for its holding, the Court largely invalidated the Bankruptcy Act of 1978 because Congress had impermissibly shifted essential attributes of judicial power from the Article III district courts to the non-Article III bankruptcy courts. 458 U.S. at 87 (plurality); *id.* at 91-92 (Rehnquist, J., concurring in the judgment).

Based on a review of case law, the four-judge plurality identified three "narrow" exceptions to the requirement that the judicial power of the United States must be vested in Article III courts: (1) "territorial courts," exercising jurisdiction over territories not within the States that constitute the United States; (2) courts-martial; and (3) legislative courts and administrative agencies created by Congress to adjudicate cases involving "public rights." *Id.* at 64-70.[3]

[3] The plurality did not attempt to provide a comprehensive definition of what constituted a "public right." The plurality nonetheless was very explicit about one category of matters that was excluded:

> The liability of one individual to another under the law as defined is a matter of private rights. Our precedents clearly establish that *only* controversies in the former category

The plurality concluded that the bankruptcy courts as constituted by the Bankruptcy Act of 1978 fit into none of those three categories and thus violated the dictates of Article III.

Justices Rehnquist (joined by Justice O'Connor) concurred in the judgment but did so on narrower grounds, limiting his finding of unconstitutionality to cases similar in nature to the case before the Court. *Id.* at 89-92. While acknowledging that Congress's power to create non-Article III courts was limited, he declined to decide whether exercise of that power should be limited to "the three tidy exceptions" enumerated by the plurality. *Id.* at 91. He nonetheless concluded that Congress had gone too far in sanctioning "the type of adjudication to which Marathon will be subjected against its will under the 1978 Act." *Id.* He concluded, "To whatever extent different powers granted under that Act might be sustained under the 'public rights' doctrine . . ., I am satisfied that the adjudication of Northern's lawsuit cannot be so sustained." *Id.*

Critically, Rehnquist's description of the salient features of the suit against Marathon makes no mention of the feature on which Petitioner and the United States rely so heavily: the fact that Marathon had not filed a

> may be removed from Art. III courts and delegated to legislative courts or administrative agencies for their determination. Private-rights disputes, on the other hand, lie at the core of the historically recognized judicial power.

Id. at 69-70 (plurality).

claim against the bankruptcy estate.[4] Petitioner is free, of course, to argue that *Northern Pipeline* should not be applied to cases in which the party objecting to the jurisdiction of the bankruptcy court has not filed a claim, but nothing in the language of either the plurality opinion or the concurring opinion supports such a limitation. To the contrary, Justice Rehnquist stated unequivocally that the "public rights" doctrine could not justify bankruptcy-court adjudication of claims of the sort that Northern Pipeline had filed against Marathon, without any indication that the result would have been different if Marathon had filed a claim against the bankruptcy estate.

Moreover, later decisions of the Court that have discussed *Northern Pipeline* have never suggested that the decision applies only to claims filed against parties that have not themselves filed claims against the bankrupt estate. For example, in *Thomas* the Court described the holding in *Northern Pipeline* as follows:

> The Court's holding in that case establishes only

[4] Rehnquist's description was as follows:

> [T]he lawsuit in which Marathon was named seeks damages for breach of contract, misrepresentation, and other counts which are the stuff of the traditional actions at common law tried by the courts at Westminster in 1789. There is apparently no federal rule of decision provided for any of the issues in the lawsuit; the claims of Northern arise totally under state law. No m method of adjudication is hinted, other than the traditional common-law mode of judge and jury.

Id. at 90.

> that Congress may not vest in a non-Article III court the power to adjudicate, render final judgment, and issue binding orders in a traditional contract action arising under state law, without the consent of the litigants, and subject only to ordinary appellate review.

Thomas v. Union Carbide Agricultural Products Co., 473 U.S. 568, 584 (1985).

Thomas, as had *Northern Pipeline*, made reference to the fact that litigants are permitted to "consent" to having their lawsuits decided by a non-Article III court.[5] But neither decision suggests that the filing of bankruptcy claim is the equivalent to granting consent or that a lawsuit filed by a debtor against a private party is suddenly transformed into a matter involving a "public right" if the party files a claim against the bankruptcy estate.

Northern Pipeline is controlling on the facts of this case and requires a finding that Article III prohibited the non-Article III bankruptcy court from rendering a final judgment on Vickie's tortious interference claim. That claim arose under Texas law and is largely indistinguishable from the tort and contract claims that Northern Pipeline asserted against

[5] Pierce did not, of course, explicitly "consent" to the bankruptcy court conducting a trial and issuing a judgment on Vickie's counterclaim. Indeed, he repeatedly objected to a trial in the bankruptcy court WLF discusses the issue of consent more fully *infra*, including Petitioner's claim that a party that files a claim against the bankruptcy estate should be "deemed" to have consented to a non-Article III trial of all counterclaims.

Marathon. Justice Rehnquist observed that "[n]one of [the Court's Article III] cases has gone so far as to sanction the type of adjudication to which Marathon will be subjected against its will under the provisions of the 1978 Act." *Northern Pipeline*, 458 U.S. at 91 (Rehnquist, concurring in the judgment). So too, none of those cases has gone so far as to sanction the highly similar adjudication to which Vickie sought to subject Pierce against his will under the 1984 Act.

A. Case Law Involving Preference Claims Does Not Support Petitioner

Petitioner and the United States rely primarily on two decisions of this Court involving the adjudication of "preference" claims in bankruptcy proceedings. Bankruptcy law historically has included provisions authorizing bankruptcy trustees to seek the repayment of such "preferences" – funds paid by the debtor in the days immediately preceding a bankruptcy filing, if the recipient did not contemporaneously provide fair equivalent value in return for the payment. None of those decisions support Petitioner's position in this case.

Katchen v. Landy, 382 U.S. 323 (1966), held that a bankruptcy court has summary jurisdiction to order the surrender of a voidable preference proved by the trustee, if the party that received the preference previously filed a claim against the bankruptcy estate. The Court held that allowing the bankruptcy court to issue such a judgment did not violate the Seventh Amendment jury trial rights of the creditor. *Id.* at 337. The United States contends that although *Katchen* arose in the narrow voidable-preference context, it

established a rule that should apply broadly to *any* bankruptcy claimant. U.S. Br. 26.[6]

A review of the Court's reasoning makes clear that the Court did not intend such a broadly applicable result. Section 57g of the bankruptcy law then in effect, 11 U.S.C. § 93(g) (1964), prohibited the allowance of a claim when the creditor had "received or acquired preferences . . . void or voidable under federal bankruptcy law," absent a surrender of any preference. Thus, the Court noted, by the terms of § 57g, when a bankruptcy trustee objects to a claim on the grounds that the creditor has received a preference, "the claim can neither be allowed nor disallowed until the preference matter is adjudicated." *Id.* at 330. Since the allowance and disallowance of claims submitted by creditors is the traditional work of bankruptcy judges, the Court saw no difficulty in permitting them to decide preference matters when necessary to complete their normal work. *Id.*. at 330-32. Moreover, once the preference matter was decided, the Court saw no difficulty in permitting the bankruptcy judge to order the return of the preference. The Court reasoned that such orders did not violate the Seventh Amendment because the creditor under no circumstances would have been permitted a jury trial in a separate suit seeking

[6] The United States relies on the Court's statement that "[b]y presenting their claims respondents subjected themselves to all the consequences that attach to an appearance." *Id* at 335. But that quotation, by itself, says nothing about what those consequences might be. As noted in the text, the narrow rationale adopted by the Court in *Katchen* makes plain that the "consequences" spelled out in that case are inapplicable outside the context of preference claims.

return of the preference item – since the bankruptcy court's earlier claims adjudication would preclude relitigation of the preference issue under normal principles of *res judicata*. *Id.* at 336-38.

The Court's reasoning thus makes clear that *Katchen* has no bearing on the Article III claims at issue here. It is true that Pierce submitted a defamation claim to the bankruptcy court. But in order to adjudicate that claim, the court had no need to decide Vickie's tortious interference counterclaim.[7] *Katchen*'s rationale for permitting the bankruptcy court to decide the preference claim (that the creditor's claim could not be resolved without deciding the preference claim) has no relevance to a case (as here) where the claim can be decided without reference to the counterclaim.

Indeed, Footnote 9 in *Katchen* appears to be designed to emphasize that the decision was not to be applied broadly in other bankruptcy situations. Rejecting arguments that its ruling violated § 23b of the former bankruptcy law, 11 U.S.C. § 46(b) (1964) (which significantly limited the trustee's choice of courts within which to prosecute an action), the Court said:

> We . . . hold that determination of claims, whether or not affirmative relief is decreed, does

[7] Indeed, as Petitioner concedes (Pet. Br. 5), the bankruptcy court granted summary judgment to Vickie on the defamation claims on the grounds that she neither ratified nor published the alleged defamatory statements (which were allegedly uttered by her Texas attorneys). By resolving the defamation claim on those grounds, the bankruptcy court entirely eliminated the overlap between the two cases.

> not constitute adjudication of a suit by the trustee, and thus it is not necessary to ascertain whether the creditor has "consented" to such determination within the meaning of § 23b. Rather, our decision is governed by the traditional bankruptcy law that he who invokes the aid of the bankruptcy court by offering a proof of claim and demanding its allowance must abide the consequences of that procedure.

Id. at 332 n.9. In other words, the Court was explaining that: (1) it was *not* holding that the filing of a bankruptcy claim constituted "consent" to the filing of counterclaims by the bankruptcy trustee; and (2) the potential negative "consequences" of filing a claim are limited to consequences that can arise from the filing of the claim itself, not those arising from a counterclaim.

The other voidable preference case relied on by Petitioner is equally unhelpful to his position. *Langenkamp v. Culp*, 498 U.S. 42 (1990), was a brief *per curiam* decision that did no more than reaffirm *Katchen*. In 1989, the Court had held in *Grandfinanciera* that when a bankruptcy trustee files a preference action against a person who has not filed a claim against the estate, the Seventh Amendment affords that person a right to a jury trial. *Grandfinanciera, S.A. v. Nordberg*, 492 U.S. 33 (1989). Relying on that decision, the Tenth Circuit held that a jury right attached even when the defendant in the preference action *had* filed a claim against the estate. The Court summarily reversed, ruling that *Grandfinanciera* did not extend that far. *Langenkamp*, 498 U.S. at 44-45. Rather, *Langenkamp* reiterated the rule it had established in *Katchen*:

permitting a bankruptcy judge to rule on preference actions filed against those who have filed bankruptcy claims (thereby precluding a jury trial) does not violate Seventh Amendment rights. The fact that the Court chose to reverse the Tenth Circuit summarily without full briefing from the parties is a strong indication that the Court did not intend to establish new law but rather was simply reaffirming its decision in *Katchen*.

B. Filing a Bankruptcy Claim Cannot Be Deemed to Constitute "Consent" to the Filing of All Counterclaims

Petitioner argues alternatively that, even if *Northern Pipeline* does not interpret the "public rights" doctrine as encompassing bankruptcy counterclaims, Pierce should be deemed to have voluntarily consented to bankruptcy court adjudication of Vickie's counterclaim by virtue of having filed a claim with the bankruptcy estate.

In support of that claim, Petitioner relies primarily on the Court's decision in *CFTC v. Schor*, 478 U.S. 833 (1986). That reliance is misplaced; nothing in *Schor* supports an argument that Pierce consented to bankruptcy court jurisdiction.

Schor addressed a federal statutory scheme under which those complaining of a violation of their rights under Commodity Exchange Act (CEA) by a registered commodity futures broker were provided a choice of two forums. They could either: (1) file an action in federal district court; or (2) apply to the Commodity Futures Trading Commission (CFTC) for an order directing the

broker to pay reparations. CFTC regulations provided that if the complainant applied to the CFTC for a reparations order, the CFTC was authorized to adjudicate a counterclaim filed broker, if the counterclaim arose out of the same transaction. At issue in *Schor* was whether the CFTC's assertion of jurisdiction over such counterclaims violated Article III.

The Court determined that Article III did not prohibit adjudication of CEA counterclaims by a non-Article III administrative agency because those who file administrative complaints are deemed to have waived their constitutional right to "an impartial and independent federal adjudication" by consenting to CFTC jurisdiction. 478 U.S. at 848-50. Petitioner cites *Schor* for the proposition that Pierce should be deemed to have waived his constitutional rights when he consented to bankruptcy court jurisdiction.

Schor does not support Petitioner's waiver/consent argument. The petitioner in *Schor* had a choice of forums within which to assert his CEA claim. Given the very close relationship between the typical CEA claim by an aggrieved consumer and the typical counterclaim by a commodities broker for payment of trading losses, the Court deemed it highly appropriate and efficient that those two claims be heard in conjunction with one another. *Id.* The consumer could have filed his CEA claim in federal court; if he had done so in *Schor*, neither the claim nor the broker's counterclaim would have been heard by the CFTC. But with full awareness of CFTC regulations providing for jurisdiction over counterclaims, the consumer filed his CEA claim with the CFTC. *Id.* Indeed, the consumer

did not object to the CFTC's exercise of jurisdiction over the counterclaim until *after* the CFTC had ruled against him. Under those circumstances, the Court held that it was appropriate to deem the consumer's voluntary choice of a CFTC forum (which all agreed provided for quicker and more efficient adjudication of CEA claims) as a waiver of his Article III rights and as consent to the CFTC's assertion of jurisdiction over the counterclaim. *Id.*

The facts in *Schor* bear little resemblance to the situation facing Pierce when he filed his defamation claim with the bankruptcy court. Unlike the consumer in *Schor*, Pierce had no alternative forums available to him; if he wanted to assert his common law defamation claim, he had no alternative to filing a proof of claim with the bankruptcy court. While Pierce had a choice in the sense that he had the option of abandoning his property right in the defamation claim, nothing in *Schor* suggests that a "choice" of that sort is sufficient to support a finding that an individual has waived his constitutional rights.[8] At most, Pierce's "choice" might

[8] As Senator DeConcini explained in proposing in 1984 an amendment to federal bankruptcy law to exclude personal injury tort claims from the bankruptcy court's claim allowance authority (an amendment that became 28 U.S.C. § 157(b)(5)), "Unlike a trade creditor who elects to do business with a particular company, the personal injury tort claimant does not choose to be injured by a particular debtor," and therefore should "have the right to have a final order entered by an Article III district judge." 130 CONG REC. S13076 (daily ed. May 21, 1984) (statement of Sen. DeConcini). Pierce did not choose to be defamed by Vickie and her Texas attorneys and thus should not be deemed to have waived his rights to final adjudication of his defamation claim (and of her counterclaim) by an Article III court simply because he chose to file

be deemed a decision to permit his defamation claim and the tortious interference counterclaim to be adjudicated in federal courts rather than in Texas state courts. But consent to a federal forum is a far cry from consent to adjudication of counterclaims (seeking hundreds of millions of dollars) by a non-Article III court. After filing his defamation claim, Pierce repeatedly stated his objection to bankruptcy court adjudication of that claim and Vickie's tortious interference counterclaim. Nothing in *Schor* suggests that such conduct should be deemed a waiver of constitutional rights.

Assertions that a litigant has waived his rights to adjudication of his claims before an Article III court arise with regularity in the context of arbitration clauses. The Court has readily accepted the proposition that a litigant has waived his right to a judicial forum by signing an arbitration clause. But the Court has made clear that such waivers are not binding unless the agreement "clearly and unmistakably requires" arbitration, *14 Penn Plaza*, 129 S. Ct. at 1466, and (in the context of labor contracts) are "explicitly stated" in the collective-bargaining agreement. *Id.* at 1465. Similarly, because Pierce never explicitly stated that he was waiving his Article III rights nor took actions that could realistically be interpreted as constituting a waiver, he cannot be deemed to have consented to bankruptcy court jurisdiction over Vickie's tortious interference counterclaim.

the claim in the only forum made available to him.

C. The Court Has Not Backed Away From *Northern Pipeline* in its Later Decisions

In two later decisions, the Court had occasion to revisit *Northern Pipeline*'s Article III holding, both times in non-bankruptcy contexts. Neither of the decisions – *Thomas* and *Schor* – represents a retreat from *Northern Pipeline*.

Thomas held that Article III did not prohibit Congress from selecting binding arbitration as the mechanism for resolving disputes among participants in the registration program established by the Federal Insecticide, Fungicide, and Rodenticide Act (FIFRA). *Thomas*, 473 U.S. at 571. But it did so in a manner that did not call into question *Northern Pipeline*'s holding. The Court concluded that Congress's establishment of a non-Article III forum for adjudicating the claims at issue – claims by pesticide manufacturers that they were entitled to data licensing fees from other manufacturers – was constitutionally permissible because the disputes at issue involved "public rights." *Id.* at 589-90. While the Court did not adopt the precise definition of a "public right" that had been proposed by the *Northern Pipeline* plurality,[9] the Court nonetheless adhered to the view that Congress generally cannot require adjudication of "private rights" before non-Article III tribunals. *Id.* at 585-86. The Court upheld the arbitration scheme created by FIFRA only because it

[9] The plurality had stated that a "public right" must, at a minimum, "arise between the government and others." *Northern Pipeline*, 458 U.S. at 69.

deemed the data licensing fees at issue to be "public rights" – because the right to such fees was created by FIFRA. *Id.* at 589-91.

Nor can *Schor* be viewed as a retreat from *Northern Pipeline*'s holding. *Schor* stated that the distinction between public rights and private rights should not always be dispositive in Article III cases. Rather, the Court stated, "The constitutionality of a given congressional delegation of adjudicative functions to a non-Article III body must be assessed by reference to the purposes underlying the requirements of Article III." *Schor*, 478 U.S. at 847. But the Court made clear that the fact that "private rights" are at issue cuts strongly in favor of a determination that the rights must be adjudicated by an Article III court. *Id.* at 854 ("[W]here private, common law rights are at stake, our examination of the congressional attempt to control the manner in which those rights are adjudicated has been searching."). The Court held that a non-Article III court may sometimes be permissible in a "particularized area of law" – such as the commodity trading disputes at issue in *Schor*. *Id.* at 852-53. Tellingly, the Court distinguished the "specialized" jurisdiction created by the CFTC with the far broader bankruptcy jurisdiction at issue in *Northern Pipeline*. *Id.* (the CFTC deals with a "particularized area of the law . . . whereas the jurisdiction of the bankruptcy courts found unconstitutional in *Northern Pipeline* extended to broadly 'all civil proceedings arising under title 11 or arising in or related to cases under title 11."). By contrasting *Northern Pipeline* in that manner, *Schor* made clear that nothing stated by the Court should be viewed as undermining the holding of *Northern*

Pipeline: Congress may not vest in a non-Article III court the power to adjudicate, render final judgment, and issue binding orders in a traditional contract action arising under state law, without consent of the litigants.

III. SECTION 157(b) PROHIBITS A BANKRUPTCY COURT FROM ENTERING A FINAL JUDGMENT ON A BANKRUPTCY ESTATE'S COUNTERCLAIM UNDER THE FACTS OF THIS CASE

Respondent has ably demonstrated that in adopting § 157(b), Congress did not intend to authorize a bankruptcy court to a enter final judgment on a bankruptcy estate's counterclaim of the sort at issue in this case. At the very least, Respondent has demonstrated that its interpretation of § 157(b) is highly plausible and should be adopted in order to avoid the serious constitutional difficulties that would arise if Petitioner's interpretation of § 157(b) were adopted.

WLF will not repeat the arguments contained in Respondent's brief. Rather, we write separately to make several additional points. First, we note that § 157(b)(2)'s list of "core" proceedings does not purport to be exhaustive. Rather, that subsection states that core proceedings include "but are not limited to" the 16 listed categories of proceedings. Thus, if the interpretation of the United States is adopted and the language of § 157(b)(1) – all core proceedings "arising under title 11, or arising in a case under title 11" – is not viewed as a limitation on the jurisdiction of bankruptcy courts, then there are *no* explicit limits on that jurisdiction. It is inconceivable that a Congress intent

on fixing the constitutional infirmities in the bankruptcy system identified by *Northern Pipeline* would have intended to create such open-ended jurisdiction in non-Article III bankruptcy courts.

Second, the legislative history leading up to adoption of the 1984 bankruptcy statute indicates a congressional decision to grant bankruptcy courts jurisdiction to adjudicate issues which they traditionally have been designed to handle, and to deny them jurisdiction over matters more traditionally handled by Article III courts and state courts. Had Congress wanted efficiency to trump all other concerns, it most likely would have granted bankruptcy judges Article III status and granted them jurisdiction to adjudicate all claims relating in any way to the debtor. But it rejected calls to grant Article III status, and spelled out a number of areas over which bankruptcy courts were to have no jurisdiction. *See, e.g.*, § 157(b)(5) (providing that all "personal injury tort and wrongful death claims shall be tried in the district court"). *Amicus* respectfully suggests that complex state-law claims of the sort asserted by Vickie in her counterclaim are precisely the sort of claims that Congress intended to be decided by Article III courts or state courts. The trial of the issues raised by the counterclaim consumed scores of trial days in both the Texas and federal courts. That type of trial is not an area of bankruptcy court experience or expertise. It is the type of trial that Congress almost certainly had in mind when it made a conscious effort to limit the bankruptcy courts' jurisdiction over "core" proceedings.

CONCLUSION

The Washington Legal Foundation respectfully requests that the Court affirm the decision of the court of appeals.

Respectfully submitted,

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CONCLUSION

The judgment of the Ninth Circuit should be affirmed.

Respectfully submitted,

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DECEMBER 20, 2010

AMICUS CURIAE BRIEF

Supreme Court, U.S.
FILED
OFFICE OF THE CLERK

No. 10-179

IN THE

Supreme Court of the United States

HOWARD K. STERN, Executor
of the Estate of Vickie Lynn Marshall,
Petitioner,

v.

ELAINE T. MARSHALL, Executrix
of the Estate of E. Pierce Marshall,
Respondent.

On Writ of Certiorari
to the U.S. Court of Appeals
for the Ninth Circuit

BRIEF OF WASHINGTON LEGAL FOUNDATION AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENT

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WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D.C. 20002

QUESTION PRESENTED

A Texas probate court upheld the validity of an estate plan and estate planning documents prepared by J. Howard Marshall, finding that he knowingly effected his estate plan free from coercion from his son Pierce Marshall. The U.S. Court of Appeals for the Ninth Circuit concluded that the findings of the Texas probate court should be afforded preclusive effect in on-going bankruptcy proceedings involving Vickie Lynn Marshall, who was married to J. Howard Marshall in the year prior to his death in 1995. Based on that conclusion, it directed that judgment be entered in favor of the Estate of Pierce Marshall on a claim against him for tortious interference with an intervivos gift. The Estate of Vickie Lynn Marshall sought review of the appeals court's decision. The Court granted review to consider the following question:

Whether, consistent with 28 U.S.C. § 157 and Article III, a bankruptcy judge may enter final judgment on a bankruptcy estate's counterclaim against an individual who has filed a claim against the estate, where: (1) the bankruptcy court lacked jurisdiction to try the individual's claim because it was a personal injury claim; (2) resolution of the counterclaim was not a necessary precursor to resolution of the individual's claim; and (3) neither the individual's claim nor the counterclaim involved "public rights" but rather raised issues of Texas law?

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INTERESTS OF *AMICUS CURIAE*

The Washington Legal Foundation (WLF) is a public interest law and policy center with supporters in all 50 States.[1] WLF defends and promotes free enterprise, individual rights, and a limited and accountable government. WLF has appeared in this Court on numerous occasions to support its view that federal law, as well as principles of federalism, require federal courts to give full faith and credit to the judgments of state courts. *See, e.g. San Remo Hotel, L.P. v. City of San Francisco*, 545 U.S. 323 (2005); *Matsushita Electric Industrial Co. v. Epstein*, 516 U.S. 367 (1996).

For multiple reasons, WLF agrees with the appeals court's conclusion that the findings of the Texas probate court should be afforded preclusive effect in these on-going federal bankruptcy proceedings. The bankruptcy court's efforts to conduct a trial and enter a final judgment on Petitioner's tort claims far exceeded the bounds of both Article III of the Constitution and federal law. WLF is concerned that if those efforts are affirmed, the strict limitations that Congress sought to place on bankruptcy court jurisdiction will have been abandoned.

WLF agrees with the appeals court's preclusion determination for the additional reason that the Texas probate court judgment, as the last unappealed

[1] Pursuant to Supreme Court Rule 37.6, WLF states that no counsel for a party authored this brief in whole or in part; and that no person or entity, other than WLF and its counsel, made a monetary contribution intended to fund the preparation and submission of this brief. All parties have consented to the filing of this brief; letters of consent have been lodged with the clerk.

judgment entered in this case, is entitled to preclusive effect. The issues that Petitioner continues to press in these proceedings were decided conclusively against it in the Texas probate court judgment. Petitioner chose not to appeal from that judgment, nor has it sought review from the Ninth Circuit's holding that the Texas judgment conclusively decided the issues that Petitioner still seeks to press. Under those circumstances, the last-in-time rule – a rule that Respondent has asserted throughout this litigation – requires affirmance of the Ninth Circuit's preclusion determination. WLF does not believe that Petitioner's forum shopping ought to be rewarded.

STATEMENT OF THE CASE

This feud over the assets of the estate of J. Howard Marshall II has spawned three court judgments.[2] A principal issue before the Ninth Circuit was whether any of those judgments should have preclusive effect in these proceedings.

The first judgment was issued by the U.S. Bankruptcy Court for the Central District of California on December 29, 2000. The bankruptcy court determined that Pierce tortiously interfered with Vickie's expectation of an *inter vivos* gift and awarded her $450 million in compensatory damages (less any

[2] Because four of the individuals involved in this dispute – J. Howard Marshall II, Vickie Lynn Marshall, E. Pierce Marshall, and Elaine T. Marshall – share the same last name, each will be referred to herein by his or her first name only. Of those four, Elaine T. (the widow of E. Peirce and the executrix of his estate) is the only one still living.

amount recovered by Vickie in the Texas Probate Court action) and $25 million in punitive damages. *See In re Vickie Lynn Marshall* ("*Marshall I*"), 253 B.R. 550 (Bankr. C.D. Cal 2000). The district court vacated that judgment on May 24, 2001; it determined that Vickie's tortious interference claim was not a "core" bankruptcy proceeding and thus that the bankruptcy court was not empowered to enter a final judgment with respect to that claim. *In re Vickie Lynn Marshall* ("*Marshall II*"), 274 B.R. 609, 633 (C.D. Cal. 2001) (as amended on June 20, 2001). Vickie's appeal from the district court's decision to vacate the judgment was rejected by the court below. *Marshall v. Stern* ("*Marshall V*"), 600 F.3d 1037 (9th Cir. 2010).

The second final judgment was issued by the Texas Probate Court on December 7, 2001. That judgment upheld J. Howard's will and his 1982 living trust as genuine, valid, and not the product of improper conduct. Ninth Circuit Excerpts of Record ("ER") 4706. The probate court also determined that it had jurisdiction over Vickie's tortious interference claim; it rejected that claim on the merits, finding that J. Howard had not intended to make a gift to Vickie from either his estate or the living trust, and thus that Pierce was entitled to his inheritance free and clear of any claim by Vickie. ER 4721, 4718. Importantly, although Vickie actively participated in the Texas probate proceedings, she never formally asserted in those proceedings that the bankruptcy court judgment should be given preclusive effect. Under Texas law (as interpreted by the district court), a judgment becomes final for preclusion purposes when, after entry of the judgment, the 30-day period for filing a motion to amend the

judgment has expired (or the period for ruling on any such motion has expired). *Scurlock Oil Co. v. Smithwick*, 724 S.W.2d 1, 6 (Tex. 1986). This Court stated that the Probate Court judgment became final for preclusion purposes on February 11, 2002. *Marshall v. Marshall*, 547 U.S. 293, 314 (2006). Vickie did not appeal from that judgment.

The third final judgment was issued by the U.S. District Court for the Central District of California on March 7, 2002. The district court concluded that Pierce tortiously interfered with Vickie's expectancy and awarded her compensatory and punitive damages totaling $89 million. *In re Vickie Lynn Marshall* ("*Marshall IV*"), 275 B.R. 5 (C.D. Cal. 2002). The district court had previously (on December 21, 2001) rejected Pierce's request that the December 7, 2001 probate court findings be given preclusive effect. *In re Vickie Lynn Marshall* ("*Marshall III*"), 271 B.R. 858 (C.D. Cal. 2001). As part of its *Marshall V* decision (Pet. App. 1-89), the Ninth Circuit concluded that the district court erred in failing to give preclusive effect to the probate court findings. In particular, the Ninth Circuit rejected Vickie's contention that the issues she was seeking to litigate in the bankruptcy proceedings were distinct from the issues decided in the probate court. *Marshall V*, 600 F.3d at 1062-64. It also determined that Vickie had "fully and fairly litigated" those issues in the probate court. *Id.* at 1063.

Before the Ninth Circuit, Respondent raised two principal arguments regarding why preclusive effect should be given to the probate court's December 7, 2001 judgment rather than to the December 20, 2000

bankruptcy court judgment. First, Respondent argued that the bankruptcy lacked jurisdiction to enter a final judgment on Vickie's state-law counterclaim under 28 U.S.C. §157(b), but rather was authorized (at most) to submit proposed findings of fact and conclusions of law to the district court under § 157(c). Second, Respondent argued that even if the bankruptcy court was acting within its jurisdiction, the last-in-time rule required that preclusive effect be given to the later judgment – in this case, the December 7, 2001 probate court judgment.

The Ninth Circuit ruled in Respondent's favor on the first argument and thus did not need to reach the second argument. The court's ruling focused on 28 U.S.C. § 157(b), the provision that grants bankruptcy courts jurisdiction to enter final judgments in certain cases. The court held that determining whether a proceeding falls within a bankruptcy court's § 157(b) jurisdiction is a "two-step" process. First, one determines whether a proceeding is a "core proceeding" within the meaning of § 157(b)(2). If so, a bankruptcy court may enter a final judgment if the "core proceeding" "aris[es] under title 11" or "aris[es] in a case under title 11." *Marshall V*, 600 F.3d at 1055.

Petitioner contended that Vickie's tortious interference counterclaim was a "core proceeding" under § 157(b)(2)(C) (which provides that core proceedings include, but are not limited to, "counterclaims by the estate against persons filing claims against the estate"). The Ninth Circuit held that regardless whether Vickie's claim was a "core proceeding," it was not a core proceeding "in a case arising under the Bankruptcy Code" because it was "not

so closely related to Pierce Marshall's defamation claim that it must be resolved in order to determine the allowance or disallowance of his claim against her bankruptcy estate." *Id.* at 1059. The court concluded that its "closely related" standard was the proper reading of § 157(b) based on: (1) its review of the evolution of the Bankruptcy Code; (2) this Court's opinions in cases construing Article III and Seventh Amendment limitations on bankruptcy court jurisdiction; and (3) Ninth Circuit jurisprudence "cautioning against creating constitutional problems through an overly broad construction" of bankruptcy court jurisdiction. *Id.* at 1058.

The Court granted review to Petitioner on the issue of whether the Ninth Circuit properly interpreted § 157(b). Petitioner did not seek review of the Ninth Circuit's holding that the issues Vickie sought to litigate in the bankruptcy proceedings were *not* distinct from the issues decided in the probate court; thus, that holding is now final.

SUMMARY OF ARGUMENT

WLF agrees with Respondent that the bankruptcy court exceeded its jurisdiction when in December 2000 it enter a judgment on Vickie's tortious interference counterclaim. But under well-established rules governing *res judicata* and collateral estoppel, the probate court judgment would be entitled to preclusive effect even if this Court reverses the district court on this issue and determines that the bankruptcy court judgment was properly entered. When (as would be true here if the bankruptcy court judgment were deemed

properly entered) conflicting judgments have been entered by two courts, the last-in-time rule requires that preclusive effect be given to the later judgment – in this case, the probate court judgment.

WLF also agrees with Respondent that the bankruptcy court, by entering a final judgment on Vickie's state-law counterclaim, exceeded the jurisdiction granted it by 28 U.S.C. § 157(b). If the Court nonetheless interprets the statute in the manner suggested by Petitioner, then it should not hesitate to rule that § 157(b) is unconstitutional as applied in this case. The Court's Article III precedent makes clear that Congress is not permitted to authorize the federal adjudication of claims of this nature by a body other than an Article III court. Nor do the facts support a finding that Respondent has waived his Article III rights by consenting to the bankruptcy court's jurisdiction.

In adopting § 157(b), Congress did not intend to authorize a bankruptcy court to a enter final judgment on a bankruptcy estate's counterclaim of the sort at issue in this case. At the very least, Respondent has demonstrated that its interpretation of § 157(b) is highly plausible and should be adopted in order to avoid the serious constitutional difficulties that would arise if Petitioner's interpretation of § 157(b) were adopted. Were the Court to adopt the interpretation of § 157(b) espoused by Petitioner and the United States, all effective limits on the jurisdiction of bankruptcy courts would be eliminated. In responding to *Northern Pipeline*, Congress made clear that it intended to impose strict limits on that jurisdiction.

ARGUMENT

I. REGARDLESS WHETHER THE BANKRUPTCY COURT WAS EMPOWERED TO ENTER A JUDGMENT, THE PROBATE COURT JUDGMENT MUST PREVAIL UNDER THE LAST-IN-TIME RULE

J. Howard Marshall II died more than 15 years ago. Litigation over the disposition of his assets has been going on for nearly as long, and it has outlived Vickie and Pierce, the two principal adversaries. It needs to end.

WLF agrees with Respondent that the bankruptcy court exceeded its jurisdiction when in December 2000 it enter a judgment on Vickie's tortious interference counterclaim. But under well-established rules governing *res judicata* and collateral estoppel, the probate court judgment would be entitled to preclusive effect even if this Court reverses the district court on this issue and determines that the bankruptcy court judgment was properly entered. When (as would be true here if the bankruptcy court judgment were deemed properly entered) conflicting judgments have been entered by two courts, the last-in-time rule requires that preclusive effect be given to the later judgment – in this case, the probate court judgment. *See, e.g.*, RESTATEMENT (SECOND) OF JUDGMENTS, § 15 (1982).

Respondent raised the last-in-time rule in both the district court and the Ninth Circuit. The appeals court did not need to reach the issue because it held that the bankruptcy court lacked jurisdiction to enter its

judgment. But "[w]ithout cross-petitioning for certiorari, a prevailing party may, of course, defend its judgment on any ground properly raised below whether or not that ground was relied upon, rejected, or even considered by the District Court or the Court of Appeals." *14 Penn Plaza LLC v. Pyett*, 129 S. Ct. 1456, 1474 (2009) (quoting *Grandfinanciera, S.A. v. Nordberg*, 492 U.S. 33, 38-39 (1989). In her brief filed in this Court, Respondent has explicitly preserved her assertion that the last-in-time rule bars Vickie's tortious interference claim. Resp. Br. 34.

The Court, in an exercise of its discretion, often declines to address an issue that has not yet been decided by the lower courts, and if necessary will remand a case to give the court of appeals the initial opportunity to consider the issue. WLF respectfully suggests that any such remand would be inappropriate under the facts of this case. This litigation is before the Court for a second occasion. The interests of justice will not be served by allowing the case to stretch into a third decade. The basic facts regarding the course of the litigation are largely undisputed. The applicability of the last-in-time rule is clear-cut. Should the Court decide that the bankruptcy court had jurisdiction to enter a judgment on Vickie's tortious interference claim, the Court should go on to determine whether the last-in-time rule operates to bar consideration of that claim.

The last-in-time rule, which provides that the most recent of two inconsistent judgments controls, faithfully applies the principles of the Full Faith and Credit Clause and its implementing Act. The Court applied the last-in-time rule to give conclusive effect to

a later-entered judgment in *Treinies v. Sunshine Mining Co.*, 308 U.S. 66, 74-78 (1939). State courts in Washington and Idaho had issued conflicting judgments regarding ownership of stock in Sunshine Mining Co. Sunshine later filed an interpleader action, seeking guidance from the federal courts regarding ownership. The Court determined that the Idaho judgment should prevail because: (1) it was issued later; and (2) the Idaho courts (before whom all parties appeared) determined that the Washington courts lacked jurisdiction over the stock and thus that the Washington judgment was not binding; (3) the party that had prevailed in the Washington lawsuit failed to appeal from the adverse Idaho decision; and (4) issue preclusion prevented the federal courts from relitigating the jurisdictional question. *Id.* *See generally* Ruth B. Ginsburg, *Judgments in Search of Full Faith and Credit: The Last-in-Time Rule for Conflicting Judgments*, 82 HARV. L. REV. 798 (1969).

The probate court can hardly be blamed for having failed to give preclusive effect to the bankruptcy judgment. By the time the probate court issued its final judgment in December 2001, the bankruptcy court judgment had long since been vacated by the district court – so there was no existing judgment to which the probate court could have deferred. But if Vickie believed that the probate court erred in failing to defer to the bankruptcy court judgment and findings, her appropriate response would have been to appeal the judgment – all the way to the U.S. Supreme Court if necessary. Instead of pursuing such an appeal, Vickie chose to pursue a collateral attack on the probate court judgment in the federal courts. The last-in-time rule

was adopted to prevent just such collateral attacks.

Moreover, Vickie never filed any papers in the probate court asserting that the bankruptcy court judgment should be given preclusive effect. She argued in the lower federal courts that she had adequately preserved the point because one of her attorneys raised the point orally on one occasion in the probate court. But even so, any such oral assertion was inadequate to: (1) excuse her failure to take a direct appeal from the probate court judgment; or (2) explain how the probate court could be deemed to have erred given that the bankruptcy court judgment had been vacated months before the probate court issued its judgment.

This case raises a wrinkle on the last-in-time rule because the first judgment (the December 2000 bankruptcy court judgment) is still on direct appeal. Commentators are nonetheless unanimous in concluding that the last-in-time rule requires an appellate court hearing a direct appeal of the first judgment to defer to the last judgment. One leading treatise concludes:

> [O]ne of the two judgments must control, and there is no reason to depart from the general preference for the second judgment if the parties have failed to assert preclusion from the first judgment or if the second court has properly rejected the preclusion argument. The court reviewing the first judgment may be tempted to review the preclusion effects of the first judgment if there was no effective opportunity to raise the question in the second action or if rejection of the

> preclusion argument seems dubious. *That temptation should be resisted.* Unless appeals from both judgments can be consolidated before a single court, the second judgment should be reviewed only within its own system. Any claim that the court reviewing the first judgment has power to enter its own subsequent judgment that should prevail over the second judgment would simply lead to a parallel assertion that review of the second judgment can lead to yet another and most final judgment.

18 C. Wright, A. Miller, & E. Cooper, *Federal Practice and Procedure: Jurisdiction*, § 4404 at 30-31 (1981) (emphasis added).

The judgment of the probate court is final, and has been for nearly a decade. Having failed to appeal that judgment, Petitioner is not entitled at this late date to ask the Court to re-examine it. The Ninth Circuit ruled that the probate court judgment conclusively determined the issues that Vickie was seeking to press in the bankruptcy proceedings, rejecting her contention that those issues were distinct from the issues decided in the probate court. *Marshall V*, 600 F.3d at 1062-64. Accordingly, the last-in-time rule provides an alternative basis for affirming the Ninth Circuit's judgment.

II. ARTICLE III BARS BANKRUPTCY JUDGES FROM ENTERING A FINAL JUDGMENT ON A BANKRUPTCY ESTATE'S COUNTERCLAIM UNDER THE FACTS OF THIS CASE

WLF agrees with Respondent that the bankruptcy court, by entering a final judgment on Vickie's state-law counterclaim, exceeded the jurisdiction granted it by 28 U.S.C. § 157(b). If the Court nonetheless interprets the statute in the manner suggested by Petitioner, then it should not hesitate to rule that § 157(b) is unconstitutional as applied in this case. The Court's Article III precedent makes clear that Congress is not permitted to authorize the federal adjudication of claims of this nature by a body other than an Article III court.

It is common ground that, in general, the judicial power of the United States must be exercised by courts having the attributes prescribed by Article III. The Constitution explicitly sets forth those attributes:

> The Judges, both of the supreme and inferior Courts, shall hold their Offices during good Behaviour, and shall, at Stated Times, receive for their Services, a Compensation, which shall not be diminished during their Continuance in Office.

Art. III, § 1. Bankruptcy judges do not and never have possessed those attributes – they are appointed for a fixed term, they can be removed from office by means other than a congressional impeachment and trial, and their salaries are not protected from diminution by

Congress. Accordingly, all agree that bankruptcy courts do not qualify as Article III courts.

In *Northern Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982), the Court imposed strict constitutional limits on the authority of non-Article III bankruptcy courts to exercise jurisdiction over state-law claims filed by a debtor-in-possession against a third party. Although the six-justice majority could not agree on the precise rationale for its holding, the Court largely invalidated the Bankruptcy Act of 1978 because Congress had impermissibly shifted essential attributes of judicial power from the Article III district courts to the non-Article III bankruptcy courts. 458 U.S. at 87 (plurality); *id.* at 91-92 (Rehnquist, J., concurring in the judgment).

Based on a review of case law, the four-judge plurality identified three "narrow" exceptions to the requirement that the judicial power of the United States must be vested in Article III courts: (1) "territorial courts," exercising jurisdiction over territories not within the States that constitute the United States; (2) courts-martial; and (3) legislative courts and administrative agencies created by Congress to adjudicate cases involving "public rights." *Id.* at 64-70.[3]

[3] The plurality did not attempt to provide a comprehensive definition of what constituted a "public right." The plurality nonetheless was very explicit about one category of matters that was excluded:

> The liability of one individual to another under the law as defined is a matter of private rights. Our precedents clearly establish that *only* controversies in the former category

The plurality concluded that the bankruptcy courts as constituted by the Bankruptcy Act of 1978 fit into none of those three categories and thus violated the dictates of Article III.

Justices Rehnquist (joined by Justice O'Connor) concurred in the judgment but did so on narrower grounds, limiting his finding of unconstitutionality to cases similar in nature to the case before the Court. *Id.* at 89-92. While acknowledging that Congress's power to create non-Article III courts was limited, he declined to decide whether exercise of that power should be limited to "the three tidy exceptions" enumerated by the plurality. *Id.* at 91. He nonetheless concluded that Congress had gone too far in sanctioning "the type of adjudication to which Marathon will be subjected against its will under the 1978 Act." *Id.* He concluded, "To whatever extent different powers granted under that Act might be sustained under the 'public rights' doctrine . . ., I am satisfied that the adjudication of Northern's lawsuit cannot be so sustained." *Id.*

Critically, Rehnquist's description of the salient features of the suit against Marathon makes no mention of the feature on which Petitioner and the United States rely so heavily: the fact that Marathon had not filed a

> may be removed from Art. III courts and delegated to legislative courts or administrative agencies for their determination. Private-rights disputes, on the other hand, lie at the core of the historically recognized judicial power.

Id. at 69-70 (plurality).

claim against the bankruptcy estate.[4] Petitioner is free, of course, to argue that *Northern Pipeline* should not be applied to cases in which the party objecting to the jurisdiction of the bankruptcy court has not filed a claim, but nothing in the language of either the plurality opinion or the concurring opinion supports such a limitation. To the contrary, Justice Rehnquist stated unequivocally that the "public rights" doctrine could not justify bankruptcy-court adjudication of claims of the sort that Northern Pipeline had filed against Marathon, without any indication that the result would have been different if Marathon had filed a claim against the bankruptcy estate.

Moreover, later decisions of the Court that have discussed *Northern Pipeline* have never suggested that the decision applies only to claims filed against parties that have not themselves filed claims against the bankrupt estate. For example, in *Thomas* the Court described the holding in *Northern Pipeline* as follows:

> The Court's holding in that case establishes only

[4] Rehnquist's description was as follows:

> [T]he lawsuit in which Marathon was named seeks damages for breach of contract, misrepresentation, and other counts which are the stuff of the traditional actions at common law tried by the courts at Westminster in 1789. There is apparently no federal rule of decision provided for any of the issues in the lawsuit; the claims of Northern arise totally under state law. No m method of adjudication is hinted, other than the traditional common-law mode of judge and jury.

Id. at 90.

> that Congress may not vest in a non-Article III court the power to adjudicate, render final judgment, and issue binding orders in a traditional contract action arising under state law, without the consent of the litigants, and subject only to ordinary appellate review.

Thomas v. Union Carbide Agricultural Products Co., 473 U.S. 568, 584 (1985).

Thomas, as had *Northern Pipeline*, made reference to the fact that litigants are permitted to "consent" to having their lawsuits decided by a non-Article III court.[5] But neither decision suggests that the filing of bankruptcy claim is the equivalent to granting consent or that a lawsuit filed by a debtor against a private party is suddenly transformed into a matter involving a "public right" if the party files a claim against the bankruptcy estate.

Northern Pipeline is controlling on the facts of this case and requires a finding that Article III prohibited the non-Article III bankruptcy court from rendering a final judgment on Vickie's tortious interference claim. That claim arose under Texas law and is largely indistinguishable from the tort and contract claims that Northern Pipeline asserted against

[5] Pierce did not, of course, explicitly "consent" to the bankruptcy court conducting a trial and issuing a judgment on Vickie's counterclaim. Indeed, he repeatedly objected to a trial in the bankruptcy court WLF discusses the issue of consent more fully *infra*, including Petitioner's claim that a party that files a claim against the bankruptcy estate should be "deemed" to have consented to a non-Article III trial of all counterclaims.

Marathon. Justice Rehnquist observed that "[n]one of [the Court's Article III] cases has gone so far as to sanction the type of adjudication to which Marathon will be subjected against its will under the provisions of the 1978 Act." *Northern Pipeline*, 458 U.S. at 91 (Rehnquist, concurring in the judgment). So too, none of those cases has gone so far as to sanction the highly similar adjudication to which Vickie sought to subject Pierce against his will under the 1984 Act.

A. Case Law Involving Preference Claims Does Not Support Petitioner

Petitioner and the United States rely primarily on two decisions of this Court involving the adjudication of "preference" claims in bankruptcy proceedings. Bankruptcy law historically has included provisions authorizing bankruptcy trustees to seek the repayment of such "preferences" – funds paid by the debtor in the days immediately preceding a bankruptcy filing, if the recipient did not contemporaneously provide fair equivalent value in return for the payment. None of those decisions support Petitioner's position in this case.

Katchen v. Landy, 382 U.S. 323 (1966), held that a bankruptcy court has summary jurisdiction to order the surrender of a voidable preference proved by the trustee, if the party that received the preference previously filed a claim against the bankruptcy estate. The Court held that allowing the bankruptcy court to issue such a judgment did not violate the Seventh Amendment jury trial rights of the creditor. *Id.* at 337. The United States contends that although *Katchen* arose in the narrow voidable-preference context, it

established a rule that should apply broadly to *any* bankruptcy claimant. U.S. Br. 26.[6]

A review of the Court's reasoning makes clear that the Court did not intend such a broadly applicable result. Section 57g of the bankruptcy law then in effect, 11 U.S.C. § 93(g) (1964), prohibited the allowance of a claim when the creditor had "received or acquired preferences . . . void or voidable under federal bankruptcy law," absent a surrender of any preference. Thus, the Court noted, by the terms of § 57g, when a bankruptcy trustee objects to a claim on the grounds that the creditor has received a preference, "the claim can neither be allowed nor disallowed until the preference matter is adjudicated." *Id.* at 330. Since the allowance and disallowance of claims submitted by creditors is the traditional work of bankruptcy judges, the Court saw no difficulty in permitting them to decide preference matters when necessary to complete their normal work. *Id.*. at 330-32. Moreover, once the preference matter was decided, the Court saw no difficulty in permitting the bankruptcy judge to order the return of the preference. The Court reasoned that such orders did not violate the Seventh Amendment because the creditor under no circumstances would have been permitted a jury trial in a separate suit seeking

[6] The United States relies on the Court's statement that "[b]y presenting their claims respondents subjected themselves to all the consequences that attach to an appearance." *Id* at 335. But that quotation, by itself, says nothing about what those consequences might be. As noted in the text, the narrow rationale adopted by the Court in *Katchen* makes plain that the "consequences" spelled out in that case are inapplicable outside the context of preference claims.

return of the preference item – since the bankruptcy court's earlier claims adjudication would preclude relitigation of the preference issue under normal principles of *res judicata*. *Id.* at 336-38.

The Court's reasoning thus makes clear that *Katchen* has no bearing on the Article III claims at issue here. It is true that Pierce submitted a defamation claim to the bankruptcy court. But in order to adjudicate that claim, the court had no need to decide Vickie's tortious interference counterclaim.[7] *Katchen*'s rationale for permitting the bankruptcy court to decide the preference claim (that the creditor's claim could not be resolved without deciding the preference claim) has no relevance to a case (as here) where the claim can be decided without reference to the counterclaim.

Indeed, Footnote 9 in *Katchen* appears to be designed to emphasize that the decision was not to be applied broadly in other bankruptcy situations. Rejecting arguments that its ruling violated § 23b of the former bankruptcy law, 11 U.S.C. § 46(b) (1964) (which significantly limited the trustee's choice of courts within which to prosecute an action), the Court said:

> We . . . hold that determination of claims, whether or not affirmative relief is decreed, does

[7] Indeed, as Petitioner concedes (Pet. Br. 5), the bankruptcy court granted summary judgment to Vickie on the defamation claims on the grounds that she neither ratified nor published the alleged defamatory statements (which were allegedly uttered by her Texas attorneys). By resolving the defamation claim on those grounds, the bankruptcy court entirely eliminated the overlap between the two cases.

> not constitute adjudication of a suit by the trustee, and thus it is not necessary to ascertain whether the creditor has "consented" to such determination within the meaning of § 23b. Rather, our decision is governed by the traditional bankruptcy law that he who invokes the aid of the bankruptcy court by offering a proof of claim and demanding its allowance must abide the consequences of that procedure.

Id. at 332 n.9. In other words, the Court was explaining that: (1) it was *not* holding that the filing of a bankruptcy claim constituted "consent" to the filing of counterclaims by the bankruptcy trustee; and (2) the potential negative "consequences" of filing a claim are limited to consequences that can arise from the filing of the claim itself, not those arising from a counterclaim.

The other voidable preference case relied on by Petitioner is equally unhelpful to his position. *Langenkamp v. Culp*, 498 U.S. 42 (1990), was a brief *per curiam* decision that did no more than reaffirm *Katchen*. In 1989, the Court had held in *Grandfinanciera* that when a bankruptcy trustee files a preference action against a person who has not filed a claim against the estate, the Seventh Amendment affords that person a right to a jury trial. *Grandfinanciera, S.A. v. Nordberg*, 492 U.S. 33 (1989). Relying on that decision, the Tenth Circuit held that a jury right attached even when the defendant in the preference action *had* filed a claim against the estate. The Court summarily reversed, ruling that *Grandfinanciera* did not extend that far. *Langenkamp*, 498 U.S. at 44-45. Rather, *Langenkamp* reiterated the rule it had established in *Katchen*:

permitting a bankruptcy judge to rule on preference actions filed against those who have filed bankruptcy claims (thereby precluding a jury trial) does not violate Seventh Amendment rights. The fact that the Court chose to reverse the Tenth Circuit summarily without full briefing from the parties is a strong indication that the Court did not intend to establish new law but rather was simply reaffirming its decision in *Katchen*.

B. Filing a Bankruptcy Claim Cannot Be Deemed to Constitute "Consent" to the Filing of All Counterclaims

Petitioner argues alternatively that, even if *Northern Pipeline* does not interpret the "public rights" doctrine as encompassing bankruptcy counterclaims, Pierce should be deemed to have voluntarily consented to bankruptcy court adjudication of Vickie's counterclaim by virtue of having filed a claim with the bankruptcy estate.

In support of that claim, Petitioner relies primarily on the Court's decision in *CFTC v. Schor*, 478 U.S. 833 (1986). That reliance is misplaced; nothing in *Schor* supports an argument that Pierce consented to bankruptcy court jurisdiction.

Schor addressed a federal statutory scheme under which those complaining of a violation of their rights under Commodity Exchange Act (CEA) by a registered commodity futures broker were provided a choice of two forums. They could either: (1) file an action in federal district court; or (2) apply to the Commodity Futures Trading Commission (CFTC) for an order directing the

broker to pay reparations. CFTC regulations provided that if the complainant applied to the CFTC for a reparations order, the CFTC was authorized to adjudicate a counterclaim filed broker, if the counterclaim arose out of the same transaction. At issue in *Schor* was whether the CFTC's assertion of jurisdiction over such counterclaims violated Article III.

The Court determined that Article III did not prohibit adjudication of CEA counterclaims by a non-Article III administrative agency because those who file administrative complaints are deemed to have waived their constitutional right to "an impartial and independent federal adjudication" by consenting to CFTC jurisdiction. 478 U.S. at 848-50. Petitioner cites *Schor* for the proposition that Pierce should be deemed to have waived his constitutional rights when he consented to bankruptcy court jurisdiction.

Schor does not support Petitioner's waiver/consent argument. The petitioner in *Schor* had a choice of forums within which to assert his CEA claim. Given the very close relationship between the typical CEA claim by an aggrieved consumer and the typical counterclaim by a commodities broker for payment of trading losses, the Court deemed it highly appropriate and efficient that those two claims be heard in conjunction with one another. *Id.* The consumer could have filed his CEA claim in federal court; if he had done so in *Schor*, neither the claim nor the broker's counterclaim would have been heard by the CFTC. But with full awareness of CFTC regulations providing for jurisdiction over counterclaims, the consumer filed his CEA claim with the CFTC. *Id.* Indeed, the consumer

did not object to the CFTC's exercise of jurisdiction over the counterclaim until *after* the CFTC had ruled against him. Under those circumstances, the Court held that it was appropriate to deem the consumer's voluntary choice of a CFTC forum (which all agreed provided for quicker and more efficient adjudication of CEA claims) as a waiver of his Article III rights and as consent to the CFTC's assertion of jurisdiction over the counterclaim. *Id.*

The facts in *Schor* bear little resemblance to the situation facing Pierce when he filed his defamation claim with the bankruptcy court. Unlike the consumer in *Schor*, Pierce had no alternative forums available to him; if he wanted to assert his common law defamation claim, he had no alternative to filing a proof of claim with the bankruptcy court. While Pierce had a choice in the sense that he had the option of abandoning his property right in the defamation claim, nothing in *Schor* suggests that a "choice" of that sort is sufficient to support a finding that an individual has waived his constitutional rights.[8] At most, Pierce's "choice" might

[8] As Senator DeConcini explained in proposing in 1984 an amendment to federal bankruptcy law to exclude personal injury tort claims from the bankruptcy court's claim allowance authority (an amendment that became 28 U.S.C. § 157(b)(5)), "Unlike a trade creditor who elects to do business with a particular company, the personal injury tort claimant does not choose to be injured by a particular debtor," and therefore should "have the right to have a final order entered by an Article III district judge." 130 CONG REC. S13076 (daily ed. May 21, 1984) (statement of Sen. DeConcini). Pierce did not choose to be defamed by Vickie and her Texas attorneys and thus should not be deemed to have waived his rights to final adjudication of his defamation claim (and of her counterclaim) by an Article III court simply because he chose to file

be deemed a decision to permit his defamation claim and the tortious interference counterclaim to be adjudicated in federal courts rather than in Texas state courts. But consent to a federal forum is a far cry from consent to adjudication of counterclaims (seeking hundreds of millions of dollars) by a non-Article III court. After filing his defamation claim, Pierce repeatedly stated his objection to bankruptcy court adjudication of that claim and Vickie's tortious interference counterclaim. Nothing in *Schor* suggests that such conduct should be deemed a waiver of constitutional rights.

Assertions that a litigant has waived his rights to adjudication of his claims before an Article III court arise with regularity in the context of arbitration clauses. The Court has readily accepted the proposition that a litigant has waived his right to a judicial forum by signing an arbitration clause. But the Court has made clear that such waivers are not binding unless the agreement "clearly and unmistakably requires" arbitration, *14 Penn Plaza*, 129 S. Ct. at 1466, and (in the context of labor contracts) are "explicitly stated" in the collective-bargaining agreement. *Id.* at 1465. Similarly, because Pierce never explicitly stated that he was waiving his Article III rights nor took actions that could realistically be interpreted as constituting a waiver, he cannot be deemed to have consented to bankruptcy court jurisdiction over Vickie's tortious interference counterclaim.

the claim in the only forum made available to him.

C. The Court Has Not Backed Away From *Northern Pipeline* in its Later Decisions

In two later decisions, the Court had occasion to revisit *Northern Pipeline*'s Article III holding, both times in non-bankruptcy contexts. Neither of the decisions – *Thomas* and *Schor* – represents a retreat from *Northern Pipeline*.

Thomas held that Article III did not prohibit Congress from selecting binding arbitration as the mechanism for resolving disputes among participants in the registration program established by the Federal Insecticide, Fungicide, and Rodenticide Act (FIFRA). *Thomas*, 473 U.S. at 571. But it did so in a manner that did not call into question *Northern Pipeline*'s holding. The Court concluded that Congress's establishment of a non-Article III forum for adjudicating the claims at issue – claims by pesticide manufacturers that they were entitled to data licensing fees from other manufacturers – was constitutionally permissible because the disputes at issue involved "public rights." *Id.* at 589-90. While the Court did not adopt the precise definition of a "public right" that had been proposed by the *Northern Pipeline* plurality,[9] the Court nonetheless adhered to the view that Congress generally cannot require adjudication of "private rights" before non-Article III tribunals. *Id.* at 585-86. The Court upheld the arbitration scheme created by FIFRA only because it

[9] The plurality had stated that a "public right" must, at a minimum, "arise between the government and others." *Northern Pipeline*, 458 U.S. at 69.

deemed the data licensing fees at issue to be "public rights" – because the right to such fees was created by FIFRA. *Id.* at 589-91.

Nor can *Schor* be viewed as a retreat from *Northern Pipeline*'s holding. *Schor* stated that the distinction between public rights and private rights should not always be dispositive in Article III cases. Rather, the Court stated, "The constitutionality of a given congressional delegation of adjudicative functions to a non-Article III body must be assessed by reference to the purposes underlying the requirements of Article III." *Schor*, 478 U.S. at 847. But the Court made clear that the fact that "private rights" are at issue cuts strongly in favor of a determination that the rights must be adjudicated by an Article III court. *Id.* at 854 ("[W]here private, common law rights are at stake, our examination of the congressional attempt to control the manner in which those rights are adjudicated has been searching."). The Court held that a non-Article III court may sometimes be permissible in a "particularized area of law" – such as the commodity trading disputes at issue in *Schor*. *Id.* at 852-53. Tellingly, the Court distinguished the "specialized" jurisdiction created by the CFTC with the far broader bankruptcy jurisdiction at issue in *Northern Pipeline*. *Id.* (the CFTC deals with a "particularized area of the law . . . whereas the jurisdiction of the bankruptcy courts found unconstitutional in *Northern Pipeline* extended to broadly 'all civil proceedings arising under title 11 or arising in or related to cases under title 11."). By contrasting *Northern Pipeline* in that manner, *Schor* made clear that nothing stated by the Court should be viewed as undermining the holding of *Northern*

Pipeline: Congress may not vest in a non-Article III court the power to adjudicate, render final judgment, and issue binding orders in a traditional contract action arising under state law, without consent of the litigants.

III. SECTION 157(b) PROHIBITS A BANKRUPTCY COURT FROM ENTERING A FINAL JUDGMENT ON A BANKRUPTCY ESTATE'S COUNTERCLAIM UNDER THE FACTS OF THIS CASE

Respondent has ably demonstrated that in adopting § 157(b), Congress did not intend to authorize a bankruptcy court to a enter final judgment on a bankruptcy estate's counterclaim of the sort at issue in this case. At the very least, Respondent has demonstrated that its interpretation of § 157(b) is highly plausible and should be adopted in order to avoid the serious constitutional difficulties that would arise if Petitioner's interpretation of § 157(b) were adopted.

WLF will not repeat the arguments contained in Respondent's brief. Rather, we write separately to make several additional points. First, we note that § 157(b)(2)'s list of "core" proceedings does not purport to be exhaustive. Rather, that subsection states that core proceedings include "but are not limited to" the 16 listed categories of proceedings. Thus, if the interpretation of the United States is adopted and the language of § 157(b)(1) – all core proceedings "arising under title 11, or arising in a case under title 11" – is not viewed as a limitation on the jurisdiction of bankruptcy courts, then there are *no* explicit limits on that jurisdiction. It is inconceivable that a Congress intent

on fixing the constitutional infirmities in the bankruptcy system identified by *Northern Pipeline* would have intended to create such open-ended jurisdiction in non-Article III bankruptcy courts.

Second, the legislative history leading up to adoption of the 1984 bankruptcy statute indicates a congressional decision to grant bankruptcy courts jurisdiction to adjudicate issues which they traditionally have been designed to handle, and to deny them jurisdiction over matters more traditionally handled by Article III courts and state courts. Had Congress wanted efficiency to trump all other concerns, it most likely would have granted bankruptcy judges Article III status and granted them jurisdiction to adjudicate all claims relating in any way to the debtor. But it rejected calls to grant Article III status, and spelled out a number of areas over which bankruptcy courts were to have no jurisdiction. *See, e.g.*, § 157(b)(5) (providing that all "personal injury tort and wrongful death claims shall be tried in the district court"). *Amicus* respectfully suggests that complex state-law claims of the sort asserted by Vickie in her counterclaim are precisely the sort of claims that Congress intended to be decided by Article III courts or state courts. The trial of the issues raised by the counterclaim consumed scores of trial days in both the Texas and federal courts. That type of trial is not an area of bankruptcy court experience or expertise. It is the type of trial that Congress almost certainly had in mind when it made a conscious effort to limit the bankruptcy courts' jurisdiction over "core" proceedings.

CONCLUSION

The Washington Legal Foundation respectfully requests that the Court affirm the decision of the court of appeals.

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Dated: December 20, 2010

PETITION FOR RE-HEARING

Supreme Court, U.S.
FILED
JUL 14 2011
OFFICE OF THE CLERK

No. 10-179

In The
Supreme Court of the United States

HOWARD K. STERN, EXECUTOR OF
THE ESTATE OF VICKIE LYNN MARSHALL,

Petitioner,

v.

ELAINE T. MARSHALL, EXECUTRIX OF
THE ESTATE OF E. PIERCE MARSHALL,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

PETITION FOR REHEARING ON SCOPE OF REMAND (SUPREME COURT RULE 44.1)

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INTRODUCTION

Petitioner seeks a rehearing as to the scope of the remand following this Court's June 23, 2011 decision, not the merits of the decision itself.

This Court's holding that a bankruptcy court lacks constitutional authority to enter a final judgment on a state law compulsory counterclaim to a proof of claim does not by itself require dismissal of Vickie Lynn Marshall's counterclaim or reversal of her $89 million district court judgment, as the operative judgment here is not the bankruptcy court judgment but the district court judgment. As this Court recognized, the district court treated the bankruptcy court judgment merely as proposed findings of fact and conclusions of law "and engage[d] in an 'independent review' of the record." Opn. 4-5. The Ninth Circuit reversed the district court judgment on the sole ground that a Texas probate court judgment was "'the earliest final judgment entered on matters relevant to this proceeding'" and "'the District Court should have 'afford[ed] preclusive effect' to the Texas 'court's determination of relevant legal and factual issues.'" Opn. 6, quoting Pet. App. 4-5.[1]

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[1] "Pet. App." refers to the appendix to Vickie's Petition For Certiorari filed August 3, 2010; "SER" refers to the Ninth Circuit supplemental excerpts of record, filed August 13, 2003 as docket entry 74.

However, Vickie has appealed the Texas probate court judgment, as have others; the judgment is therefore subject to reversal. That fact creates the manifest risk that Vickie could be stripped of her district court judgment because of the preclusive effect of a Texas judgment that ends up being reversed on appeal – a "grotesque result," as a leading treatise calls it. 18A Charles Alan Wright & Arthur R. Miller, *Federal Practice and Procedure* § 4433 (2d ed. 2002). Happily, this Court's own case law as well as settled law in both the federal courts and Texas support the prudent course of leaving Vickie's judgment open pending the resolution of the Texas appeal. Rehearing is thus requested so that this Court can direct the Ninth Circuit to stay this appeal pending the resolution of Vickie's Texas appeal.

THE NINTH CIRCUIT SHOULD BE DIRECTED ON REMAND TO STAY THIS APPEAL PENDING THE RESOLUTION OF VICKIE'S APPEAL OF THE TEXAS PROBATE COURT JUDGMENT SO AS TO AVOID PERPETUATING A JUDGMENT RESTING ON NOTHING MORE THAN A SUBSEQUENTLY REVERSED JUDGMENT.

A. Vickie's Appeal Seeking Reversal Of The Probate Court Judgment Is Pending In Texas.

Vickie timely appealed the probate court judgment, as did other parties, and the appeal remains pending in the Texas First Court of Appeals, although it has been stayed due to another party's bankruptcy. Tex. 1st Ct. App. case information, http://www.1stcoa.courts.

state.tx.us/opinions/case.asp?FilingID=83346 (last visited July 11, 2011).

Vickie's Texas appeal is prefigured in her trial and post-trial motions. SER 10353 & n.1; *see* Texas Rules App. Proc., Rule 33.1. There, among other grounds, she showed that the judgment entered against her was improper as a matter of law because Pierce's counterclaim for declaratory relief (the only claim that formed the basis of the judgment against her) was filed without leave of court, was filed after she had already dismissed all her affirmative claims, was not supported by the pleadings or jury findings and did not state a justiciable controversy. SER 10353-95.

If Vickie prevails on any of these grounds, the judgment as it relates to her would be reversed, and as explained below it could have no preclusive effect on her tortious interference claim.

B. The Ninth Circuit Should Be Ordered To Stay This Appeal Because If Vickie's Texas Appeal Reverses The Probate Court Judgment, Thus Rendering It Null And Void For Preclusion Purposes, The Ninth Circuit's Preclusion-Based Reversal Of The District Court Judgment Should Not Stand, And Nothing Else Can Ensure That Result.

The Ninth Circuit reversed the district court judgment on the sole ground that all the elements of preclusion had been satisfied and the district court

therefore erred in not affording issue-preclusive effect to the Texas probate court judgment. Opn. 6.

But "[s]ubstantial difficulties result from the rule that a final trial-court judgment operates as res judicata while an appeal is pending," and "a second judgment based upon the preclusive effects of the first judgment should not stand if the first judgment is reversed." Wright & Miller, *supra*, § 4433.

This is settled Texas law. *Scurlock Oil Co. v. Smithwick*, 724 S.W.2d 1, 6-7 (Tex. 1986) ("[a] judgment in a second case based on the preclusive effects of a prior judgment should not stand if the first judgment is reversed"); *Jackson v. Smith Sec. Servs., Inc.*, 786 S.W.2d 787, 788 (Tex. App. 1990) (same).

This is also settled federal law. In *Butler v. Eaton*, 141 U.S. 240 (1891), for example, this Court reversed a federal judgment that had given preclusive effect to a prior state-court judgment that was subsequently reversed by this Court. *Id.* at 241-43. Having been reversed, the state-court judgment was "subverted and rendered null and void for the purpose of any such [preclusion] defense" in the federal action. *Id.* at 242-43. While preclusion had been an effective defense below, its effectiveness was "now entirely annulled." *Id.* at 243-44.[2]

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[2] See also *Erebia v. Chrysler Plastics Prods. Corp.*, 891 F.2d 1212, 1215 (6th Cir. 1989) ("Where the prior judgment, or any part thereof, relied upon by a subsequent court has been reversed, the defense of collateral estoppel evaporates"); *Ornellas*

(Continued on following page)

A judgment that rests solely on the preclusive effect of another judgment still on appeal should "not stand if the first judgment is reversed," and that "result should *always* be avoided." Wright and Miller, *supra*, § 4433 (emphasis added). Courts ensure "full protection against the grotesque result of perpetuating a judgment that rests on nothing more than a subsequently reversed judgment" by "delaying further proceedings in the second action pending conclusion of the appeal in the first action," *id.*, by "stay[ing] its own proceedings to await the ultimate disposition of the judgment in the trial court or on appeal," Restatement (Second) of Judgments § 16, comment b (1982), or by "hold[ing] open the appeal in the second action until the determination of the appeal in the first action," *Jackson*, 786 S.W.2d at 788; *see In re Prof'l Air Traffic Controllers Org. (PATCO)*, 699 F.2d 539, 544 & n.18 (D.C. Cir. 1983) (Ginsburg, J.) (citing Restatement §16, comment b for the proposition that a court that is "asked to accord a judgment preclusive effect may be well-advised to stay its own proceedings to await the ultimate disposition of the judgment on appeal"); *Martin v. Malhoyt*, 830 F.2d 237, 264 (D.C. Cir. 1987) (Ginsburg, J.) (before applying preclusion, "care should be taken in dealing with judgments that are final, but still subject to direct review").

---

v. Oakley, 618 F.2d 1351, 1356 (9th Cir. 1980) ("A reversed or dismissed judgment cannot serve as the basis for a disposition on the ground of res judicata or collateral estoppel.").

This case particularly requires the issuance of an order staying the appeal because there is no other mechanism that would ensure adequate relief in the event that Vickie's appeal reverses the probate court judgment. Ordinarily, a party may seek relief in the district court from a final judgment "if it is based on an earlier judgment that has been reversed." Fed. R. Civ. P. 60(b)(5). However, that remedy would be insufficient here because if the district court judgment is dismissed, Elaine Marshall, the executor of Pierce's probate estate, could distribute all assets and close the estate. Tex. Prob. Code, §§ 149E, 151. Not only would the assets be gone, but so would the judgment debtor.

Thus, this Court, in its remand order, should direct the Ninth Circuit to stay this appeal pending the resolution of Vickie's Texas appeal.

CONCLUSION

For all the foregoing reasons, Vickie requests that this Court direct the Ninth Circuit on remand

to stay this appeal pending the resolution of her appeal of the Texas probate court judgment.

Dated: July 14, 2011

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CERTIFICATE OF COUNSEL

As counsel for the petitioner, I hereby certify that this petition for rehearing is presented in good faith and not for delay and is restricted to the grounds specified in Rule 44.1.

_____

Counsel for Petitioner